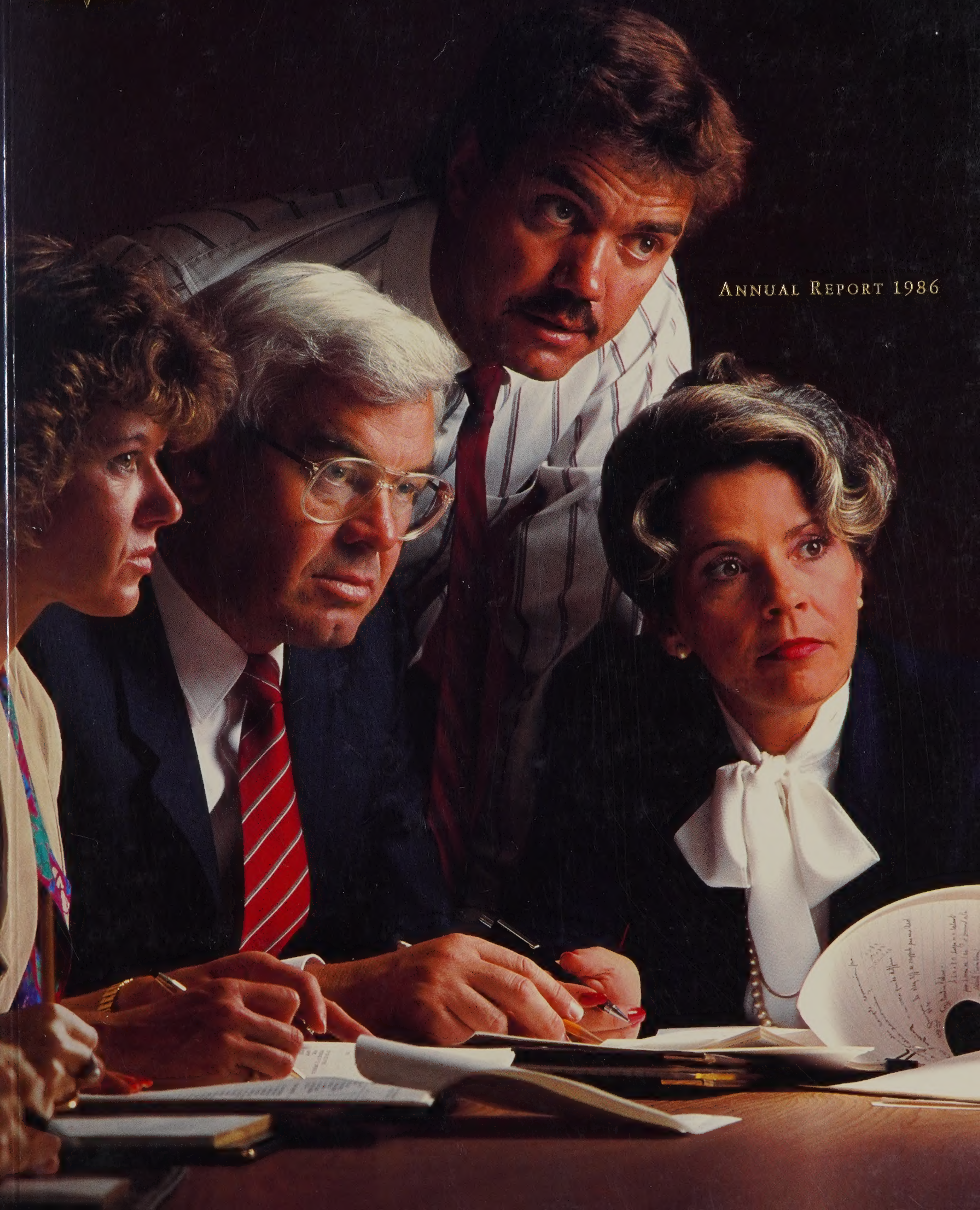
THE ROYAL BANK OF CANADA

ANNUAL REPORT 1986



Contents

Cover

Teamwork – pictorial theme of this Annual Report – is exemplified by a planning meeting in Montreal involving branch, field headquarters and corporate head office staff. Branch manager Charmaine Aubut (R), with her retail and operations manager Dan Théorêt (standing), goes over plans for a special pilot project. They work closely with Quebec retail banking vice-president Roland Guay, head office planning officers Kathy Cooper (L) and Alberta Cefis, and assistant branch administration manager Claude Lebrun (back cover).

The Royal Bank of Canada, chartered in 1869, is Canada's largest bank, with assets at the end of fiscal 1986 of $99.6 billion. Two fundamental goals are paramount: excellence in financial service across Canada and vigorous participation in selected international financial markets.

The Royal Bank's extensive network of branches, subsidiaries and affiliates comprises more than 1600 operating units in 45 countries. One of the world's largest retail banks, the Royal is also North America's sixth largest bank overall.

Corporate Headquarters is in Montreal, with certain head office functions in Toronto and Winnipeg. To bring prompt decision-making close to clients, the Bank's operations are managed through ten field headquarters worldwide.

The Bank's domestic operations include 1170 electronic Personal Touch Banking machines and a network of 1442 branches serving individuals, businesses and communities across the country, many specializing in particular market sectors.

The Bank's international operations account for more than a third of its assets. Global coverage is provided by more than 170 commercial, wholesale, investment banking, treasury and retail operating units and through more than 5000 correspondent banking relationships in nearly every country in the world.

The Royal Bank is a leader in the application of new technologies for efficient operational management and for making possible a variety of sophisticated new services.

Royal Bank management believes that success is best achieved through providing the highest quality retail and wholesale banking services where clients need them. To that end, the Bank focusses on the selection, training and development of its staff and puts a heavy premium upon responsiveness, innovation, skill and knowledge, as well as judgment, integrity and the highest standards of ethics and social responsibility.

First Quarter

- Royal Bank common shares begin trading on the major Swiss stock exchanges in Geneva, Zurich and Basle.
- The Bank acquires ownership of and exclusive rights to operate the Diners Club credit card business in Canada.
- The Bank connects its Personal Touch Banking machines with a 10,000-machine network in the United States operated by Plus System Inc.

Second Quarter

- The Bank expands its capital with a Cdn. $150 million issue of preferred shares.
- National Mutual Royal Bank, jointly owned by the Bank and the National Mutual Life Association of Australasia, opens for business in Australia.
- Orion Royal Bank Ltd., our investment banking subsidiary, completes acquisition of Kitcat & Aitken, the London stockbroker, and RBC Gilts is established.

Third Quarter

- Allan R. Taylor succeeds Rowland C. Frazee as Chairman and Chief Executive Officer, and the Bank's top management structure is realigned.
- The Bank expands its base capital with a U.S. $300 million issue of floating-rate, 99-year debentures.
- Personal Touch Banking machines are linked with a new 2,500-machine network in Canada operated by Interac.

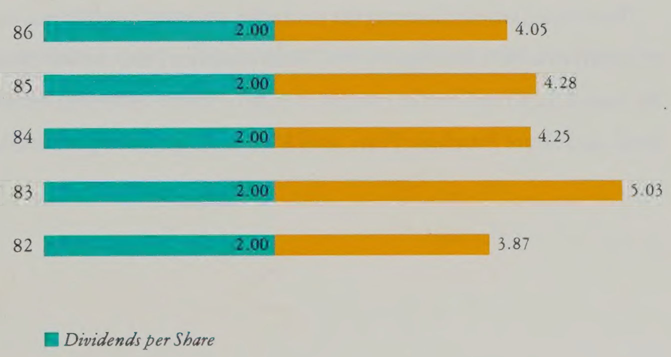
Fourth Quarter

- The Bank issues 3 million common shares, worth Cdn. $102 million, bringing total capital to $6.7 billion at October 31, 1986.
- The Bank's common shares are listed for trading on the Tokyo Stock Exchange.
- John R. Sanders is appointed Chairman and Chief Executive Officer of Orion Royal Bank Ltd.
- National Mutual Royal Bank obtains approval for a merger with the United Permanent Building Society, laying the foundation for Australia's 5th largest bank.

For the year ended October 31	*1986*	*1985*	*Per Cent Change*
Earnings Data			
Net income ($ millions)	**$489**	$488	0.2%
Return on (average) assets	**.50%**	.53%	(5.7)
Return on (average) equity	**12.0%**	13.5%	(11.1)
Balance Sheet Data ($ millions)			
Total assets	**$99,607**	$96,017	3.7
Loans	**65,934**	63,831	3.3
Deposits	**84,253**	83,543	0.8
Debentures	**2,068**	1,749	18.2
Capital and reserves	**4,662**	4,168	11.9
Capital Adequacy Ratios			
Base capital ratio	**4.2%**	3.7%	13.5
Base capital equivalent ratio (base plus 1/3 supplementary)	**4.7%**	4.2%	11.9
Adjusted total capital ratio	**5.8%**	5.3%	9.4
Common Stock Data			
Income per share			
Basic	**$4.05**	$4.28	(5.4)
Fully diluted	**3.74**	3.91	(4.3)
Dividends per share	**2.00**	2.00	—
Share price:			
High	**35.25**	32.38	8.9
Low	**27.50**	27.50	—
Close – October 31	**33.25**	31.50	5.6
Book value – October 31	**34.14**	33.10	3.1
Number of:			
Shareholders (common)	**89,752**	89,947	(0.2)
Common shares outstanding (thousands)	**106,522**	99,427	7.1
Employees	**38,186**	37,430	2.0
Branches	**1,496**	1,494	0.1
Automated banking machines	**1,170**	898	30.3

TOTAL ASSETS
(at October 31)
($ Billions)

EARNINGS PER SHARE
(Basic)
($)



This is my first Annual Report to shareholders as Chairman and Chief Executive Officer and, at the outset, I want to acknowledge the lasting contributions made to the Royal Bank by my predecessor Rowland C. Frazee. He retired last May after a distinguished 38-year career with the Royal Bank. A tribute to his achievements appears on page 75 of this report. More telling than those words is the fact that the basic strategy which Mr. Frazee helped us develop remains in place.

While stability is a widely noted strength at the Royal Bank, the capacity to adapt rapidly and smoothly to change is also a critical attribute. With this in mind, responsibilities of the most senior management team were realigned last June to reflect the changing needs of clients in our diversified markets. An important change was to replace the traditional division of the Bank between International and Domestic groups with Bank-wide mandates for the management of each of our principal businesses.

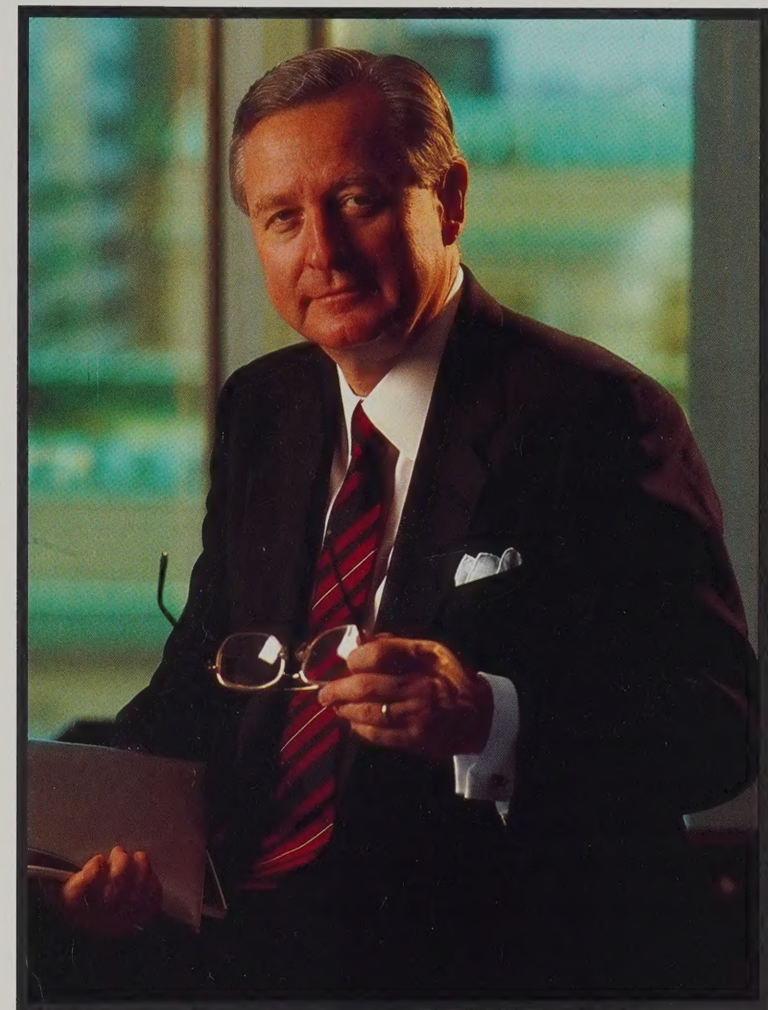
J.E. Cleghorn, President, manages our banking network worldwide. A.H. Michell, Vice-Chairman, oversees corporate resource management, including finance and the technological underpinnings of electronic banking systems. R.G.P. Styles, Vice-Chairman, oversees our global Corporate/Investment Banking and Treasury Group. R.C. Paterson, Senior Executive Vice-President, is responsible for Investment Banking in North America and Treasury. M.J. Regan, Senior Executive Vice-President, manages marketing and product development for our retail and commercial banking businesses. B.D. Gregson, Senior Executive Vice-President, has Bank-wide responsibility for credit risk management.

The central goal of the management team is to build on our track record for top-flight customer service. By serving customers well, we aim over time to substantially improve profitability–specifically to attain a return on assets of .75% and a return on equity of 16%.

In 1986, progress towards these goals was constrained, principally by the unexpected decline in world oil prices and the impact this had on the earnings of our clients in the energy sector. Their difficulties were reflected in the Bank's loan loss experience.

We did, however, benefit from several positive factors. Most notable was the Bank's continuing strong performance in the Canadian personal banking market–the backbone of our operations. Another strength, evident in the year's results, is our ability to generate fee income, which now accounts for almost a quarter of total net revenue and helps to counterbalance the effects of relatively slow commercial asset growth. Fee income from retail banking services and foreign exchange trading operations were key earnings contributors. As well, fee-generating services will increasingly play a vital role in helping to build strong, lasting and profitable relationships with customers.

These fundamental strengths underlie investor confidence in our future performance, reflected in a 14% increase in the Bank's capital base, which totalled $6.7 billion at year end. We raised $230 million in common equity, more than half of it from the Shareholder Dividend and Share Purchase Plan, and $567 million from preferred share and debenture issues.



Allan R. Taylor
Chairman & Chief Executive Officer

While our financial results inevitably fluctuate with economic conditions, it is important to take a longer term view of the Bank's business performance.

We are building for the future in ways keyed to underlying financial market trends. The internationalization of financial markets, regulatory change, technological and product innovation are all significant examples of such trends. All are contributing to intensified competition. In every market served by the Royal we have witnessed a proliferation in the number and variety of financial institutions, product lines and service delivery methods.

Given this environment, two key factors—financial services regulation and our own business strategy—merit a more detailed review.

Financial Services Regulation

While the Royal Bank Group has an international reputation in investment banking, our ability to offer even basic investment banking service in Canada has been severely limited by regulation. There were, however, extremely encouraging signs late in the year that this will change in 1987. The pressing need for such progress illustrates why we have a clear interest, as do our customers, in the continuing national debate on regulation of the financial services industry. Two key issues are on the agenda: the ground rules for competition and the need for public confidence in financial institutions.

With regard to competition, the central issue is when and how various types of financial institutions will be granted powers to offer a broader range of financial services and products. The Royal Bank has continued to stress that chartered banks, with their extensive branch and electronic delivery networks, provide more Canadians with easy access to service than any other financial industry sector. For this reason, we believe banks should be granted expanded business powers at the same time as other institutions–insurance, trust, investment banking and brokerage firms. This, in fact, was a key thrust of government policies regarding financial services, announced in December.

As financial institutions expand into new markets, the public must have *confidence* both in their management practices and in their financial soundness. Therefore, we believe all financial institutions of a certain size should be widely owned–as are the major Canadian chartered banks. A broad investor base provides an essential safeguard against the possibility of self-dealing by dominant shareholders. Another priority should be the reform of our deposit insurance system to reflect more accurately the level of risk in each financial industry sector.

Public attention has continued to focus on the financial soundness of banks. A positive step forward was the report, issued in November, of the federal Royal Commission of Inquiry into the failures of The Canadian Commercial Bank and Northland Bank. Justice Willard Estey of the Supreme Court of Canada concluded that these banks were exceptional cases, together representing only about one per cent of Canadian banking assets. His report emphasizes that these cases were *not* representative of management practices in the banking industry as a whole, stating: "The major banks, representing about 96 per cent of the assets of the industry, continue as world-scale banks whose strength and leadership is today recognized on the international stage of banking."

The Royal Bank's position in the debate on regulatory issues is consistent with its business strategy. Our priorities are expansion into Canadian investment banking and computer-based financial services.

Expanding into such new service areas is vital to one of our central corporate goals: to be recognized by our customers as a consistent leader in the value of our products and customer service. Commitment to quality service is a distinctive Royal Bank trademark, and to build on that strength we must continue to expand our range of services to meet growing customer needs.

Business Strategy

To attain these goals, we further refined our business strategy last June, concurrent with the realignment of top management responsibilities. The strategy covers such areas as risk management and credit quality, technology and management information, the use of more aggressive marketing and selling methods, specialization by market segments, and expanding our range of financial services.

Two thrusts lie at the heart of our strategy. One is outward-looking – to focus more closely on customers and their specific needs. This means delivering services, new or traditional, to the right people at the right time, in the ways they find most convenient. We are moving to develop a longer term view of key markets, to adjust product lines so that they better fit those markets and then to ensure that Bank delivery networks give our people a "direct line" to the customer.

The other thrust is inward-looking – to streamline our organization, control operating costs and to ensure that our head office support groups and "back office" pull together efficiently with our front-line customer service and sales staff. In our view, efficiency and improved customer service are mutually reinforcing.

Our strategy has been widely communicated across the Bank, through considerable direct discussion supported by a special issue of the employee magazine and the use of video. The process continues, with staff in all units participating in the process of implementing our action plans.

Longer term market trends demand that the Royal Bank set for itself ambitious goals. Given the right regulatory climate, we plan to move from being Canada's largest chartered bank to become this country's leading provider of financial services, while remaining a prominent force in selected international markets.

To achieve this, we will continue to innovate aggressively in such areas as product development, technology, training and service delivery techniques. These initiatives alone, however, cannot guarantee success. In a service business such as ours, success will depend ultimately on the human equation – the special relationship of caring professionalism linking Royal Bank people to our customers.

Allan R. Taylor
Chairman & Chief Executive Officer

The Royal Bank's distinctive reputation in the marketplace for convenient, consistently high quality *customer service* is, we believe, the basis of competitive strength. Our franchise has been built on keen sensitivity to customer needs and this remains our principal focus.

With competition intensifying, the Bank is enhancing customer service with innovative products, expanding electronic banking networks and ever more precise targeting of services to specific customer groups—whether they be multinational corporations, fledgling entrepreneurs, travellers in need of cash, or retirees seeking secure investments.

Our reputation for service has been earned by front-line staff—a sales force of customer service representatives and personal loans officers, commercial account managers and investment bankers—who understand customer needs. Less visible, but equally important to effective service, are the skills and dedication of the "back office" staff who provide critical operational and administrative support, and keep automated systems running smoothly.

3

Realignment of the Bank's senior management structure in 1986 reinforced ongoing improvements in service delivery, and in product development and marketing. One key objective was to shorten the lines of communication, and reduce management layers, between corporate head office and field management of the banking network. Our field general managers worldwide now report directly to the President, with corporate direction of Canadian and international field headquarters focussed in a single head office network management unit.

This group oversees a host of other initiatives to adjust the delivery network—more than 1600 branches and operating units, 1170 Personal Touch Banking machines, and direct electronic links with business clients' computers—to create more flexibility and an even better fit with customer needs.

Another objective of the organizational changes is to enhance sales performance. Vital support to front-line staff is provided by head office product development and marketing specialists, who monitor competitor activity, demographic trends and business conditions through intensive market surveys. They make imaginative use of this information to design the product/service mix and to prepare marketing plans and materials.

The Product Management and Marketing Group specializes in the same key market segments as our sales and service staff in branches and commercial account management units. The main segments are: personal and private banking; independent business and agriculture; and commercial banking.

To focus on the needs of multinational corporations, governments and their agencies, and correspondent banks, the Corporate/Investment Banking and Treasury Group has been formed. It brings together our corporate account managers, investment bankers and treasury traders. This initiative came in direct response to strong demand from corporate and government clients for a combination of sophisticated commercial banking products with capital markets services, such as swaps, options and innovative underwriting services.

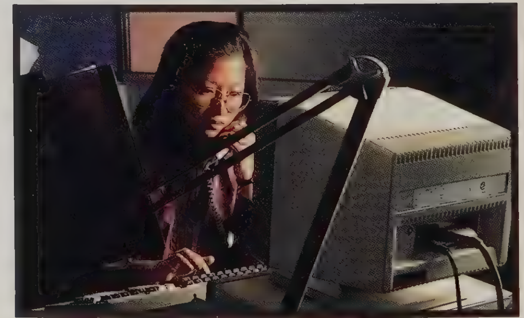
1

Teamwork is essential to managing the Royal Bank's varied operations. With our market presence reaching from the Canadian corner branch to financial centres like London and Tokyo, chairman and chief executive Allan Taylor (photo 1) works closely with six colleagues, each responsible for a specific part of the business. Together, this group forms an executive committee, our senior strategy team. Reviewing business plans are (L R): vice-chairman Mike Michell; Taylor; president John Cleghorn; and vice-chairman Geoff Styles. Discussing risk factors in investment banking with Styles (2) are senior executive vice presidents Brian Gregson and Rob Paterson (R). Electronic banking strategy brings Michell together with senior executive vice-president Joe Regan (3) for a planning session.

2

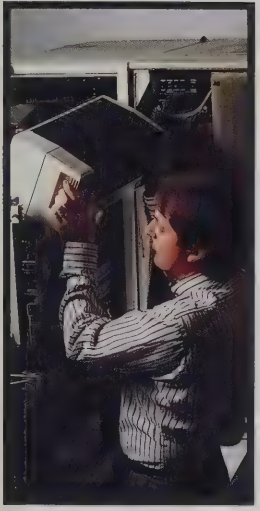
1

Our customers now enjoy convenient access to their accounts through more than 13,000 banking machines across North America. Making this possible are extensive behind-the-scenes efforts by a variety of Royal Bank people. Among them are head-office electronic banking experts (1) Dennis Graham, Susan Orr-Mongeau and Luther Carver (R), who prepared customer information and marketing programs for the launch of two shared banking-machine networks. Efficient payments processing for the new services happens at our Toronto operations centre (2), where Vivian Chow helps track an average of 30,000 transactions a day involving other financial institutions in Canada's Interac network and the Plus System network in the U.S. In Montreal (3), Douglas Johnston keeps a Personal Touch Banking machine working smoothly and well stocked with cash.



2

The group is building on our well-developed banking relationships with major private and public sector clients, our leadership in Canadian foreign exchange, money and swap markets, and our strong position in overseas capital markets. As well as serving clients, the Treasury group continues to serve as ''banker to the Bank,'' managing wholesale funding, the investment portfolio and new capital issues. Treasury strategists apply strict standards of prudence to trading operations in order to maintain ample liquidity, limit foreign exchange exposure and control interest-rate sensitivity ''gaps'' between assets and liabilities.



3

With 24-hour electronic banking the norm for many consumers and corporate treasurers, automated operational support is vital to customer service as well as to productivity improvement. Technology specialists in the Operations and Systems group work closely with business units to design new services and enhance existing ones.

This group also manages the huge volume of transaction processing handled by 25 data centres, three Visa centres and 6600 terminals in our Canadian branches. Each day, we process an average of 4 million cheques, 1 million card transactions and 1 million on-line branch transactions.

The Credit Risk Management Group specializes in overall management of the Bank's credit risk exposure, making a vital contribution to our profitability and business strategy. Key responsibilities include establishing credit policies and standards, credit training for account managers, approving major loan proposals, and negotiating loan restructurings with troubled corporate and sovereign borrowers. Significant progress has been made in the use of automated risk monitoring systems.

Whether judging credit quality or planning a sales campaign, our staff are supported by extensive training programs, which feature a mix of classroom work, outside courses and on-the-job training. Corporate personnel specialists work with business units in developing the programs, which cover numerous specialized disciplines as well as general management skills. One new training initiative, for example, encourages increased staff participation and teamwork within individual work units.

As well, the Staff Suggestion Program encourages the search for cost savings, new sources of revenue and ways of streamlining complex banking procedures. Since 1983, when the program was revamped, employee and pensioner award winners have received a total of $440,000 for suggestions, with an estimated total in reduced costs and increased revenue of $19 million.

Our staff's commitment is further reinforced by the Royal Employee Savings and Share Ownership Plan, launched in 1985. Employee shareholders now number some 17,800, or half of our Canadian staff.

Following is a review of operations and business conditions in each of the Bank's principal markets.

Personal Banking

The Bank's success in highly competitive personal banking markets rests on two key strengths: the reach of its service delivery network, and the depth of its product development and marketing expertise. The delivery network consists of people, branches, data processing centres and electronic facilities that together serve 6.5 million customers. Bank marketing experts design and package the products and services delivered.

In Canada during fiscal 1986, active real estate markets, growth in consumer spending and stable interest rates stimulated growth in demand for residential mortgages, personal loans and credit card services. At the same time, competition intensified. Canadian consumers were offered a wider range of choice through aggressive marketing and pricing strategies by a variety of financial institutions.

A significant achievement for the Royal was the growth in personal deposits to $41 billion from $39 billion worldwide. These core deposits provide a stable funding base for lending activities, thus strengthening our competitive position. We maintain a lead in deposit services by offering a broad range of savings options and, equally important, convenient service through 1442 branches and our automated banking machine network, which is the largest in Canada and among the largest in North America.

The Royal today complements more conventional bank deposit service with an array of other "investment" options, including mutual funds, money market instruments, discount brokerage services and retirement investment products. By offering an ever expanding range of choice, we are fast becoming a much more broadly-based provider of financial services to consumers.

Personal banking operations have been a consistent source of loan growth in recent years. In 1986, the Bank's home-ownership mortgage portfolio, the largest in Canada, grew at a record annual rate of more than 25%. Some 77,000 new mortgages were committed for a record amount of $4.6 billion.

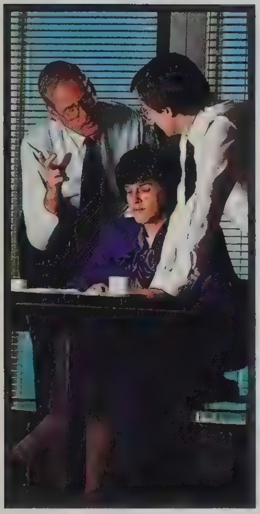
Last year, the Royal became the first to offer home buyers a "pre-arranged" mortgage on a formal basis. As well, weekly, bi-weekly and semi-monthly payment options were added to our comprehensive mortgage package. Other features include: flat-fee mortgage appraisal/application and switching; allowing customers to transfer their existing Royal Bank mortgages to newly-purchased homes; and optional group life insurance on mortgage balances at premiums lower than those offered by other lenders.

Product innovation helped the Bank to increase its substantial share of car loans last year. This was accomplished in a market in which the major automobile manufacturers, through their financial subsidiaries, offered deep interest rate discounts to move inventories of a wide range of models.

Early in the year, the Royal introduced "Shock Absorber," which offers car buyers protection against first-year depreciation loss in the event of accident or fire. The combination of Shock Absorber with the existing Buy-Back Car Loan option, also unique to the Royal, gave lending staff a powerful marketing tool. The Bank's portfolio of car loans increased 12% in the year.

Top customer service and product innovation help make us Canadian leader in credit card services. In Barrie, Ontario, marketing representative Jim McGirr (L) calls on Radio Shack store manager John McEachern to check on a new Royal Visa terminal, which cuts waiting time for customers while providing merchants with same-day credit for Visa sales.

It was an active year for credit card operations, highlighted by the introduction of the first proprietary merchant sales draft capture system in Canada. This system utilizes specially-designed Royal Bank Visa terminals which provide instant credit card authorization while automatically depositing the amount of sales to merchants' bank accounts. The Bank has the most extensive network of conventional authorization terminals of any financial institution in Canada. Our Visa card program is the largest in the country and among the largest in the world.



In Toronto, corporate card sales manager Jim Munro (L) explains to Gerald Ranking and Linda Adlam of the Canadian Bar Association-Ontario how Royal Bank Diners Club card can help professionals, like lawyers, keep better track of expenses and benefit from reduced rates at hotels and restaurants.

Considerable management effort and resources were devoted during 1986 to raising the visibility and acceptance of the Canadian Diners Club expense card, purchased by the Royal in late 1985. It complements Visa's mass-market appeal with a travel and entertainment business-expense card service expressly tailored for business and professional people.

The Royal is one of the largest users of consumer market research among financial institutions in North America. Combined with staff knowledge, research helps identify gaps in existing services, and heightens the impact of advertising, direct mail and telemarketing campaigns. As well, information about specific customer groups allows market segmentation and guides the development of matching products and services.

For higher-than-average-income individuals, a comprehensive package, Royal V.I.P. Service, was designed and successfully introduced last year. A flat monthly fee covers a host of services including personal credit lines, overdraft protection and the new gold premier Visa card. The Bank also has established private and executive banking centres in larger Canadian cities to meet the needs of high net worth clients. Private banking extends beyond Canada, with units in the Channel Islands, Geneva and the Bahamas providing highly successful funds management and trustee services through offices in strategic locations worldwide.

For Canadians planning their retirements, a pensioner's "staff suggestion" led to the creation of a special sales force of retired Royal Bankers to market retirement investment products part-time. This initiative won the Royal an international bank marketing award. More importantly, it was highly successful in business terms.

In addition to "target marketing," the Bank is reshaping its delivery network to increase service efficiency, selling capability and productivity. Branch organization is being modified to give more authority to local management teams who know their market areas intimately. Routine paperwork is increasingly being transferred from branches to centralized administrative centres, and personal computers are being specially programmed for use in speeding up loan approvals and the opening of new accounts. The aim is to allow branch staff to concentrate on serving customers and selling the Bank's rapidly expanding range of financial services.

The past year saw several milestones in the relatively short history of electronic banking at the Royal Bank. Monthly transactions handled by Personal Touch Banking machines passed the 10 million level and volume for the year topped 115 million. These volumes, among the highest per machine anywhere in the world, attest to the popularity of 24-hour convenience banking via automated banking machines.

The Bank's network expanded to 1170 banking machines from 900 at year end 1985. Included were 93 new "CashCounters," for cash withdrawals only. Smaller in size than full-service machines, these units are installed in high-traffic retail outlets such as gasoline service stations and convenience stores, many of which are open 24 hours per day.

3

Another significant milestone during 1986 was the launch of Interac, a shared banking machine network which will eventually include nearly 4000 automated banking machines for cash withdrawals involving nearly every Canadian financial institution. This has provided increased convenience for clients and is expected to be a substantial fee generator for the Royal Bank because of the size and geographic distribution of our network, which is now being used by large numbers of clients of other financial institutions.

Royal Bank clients also enjoy convenient access to their accounts through more than 10,000 machines in the Plus System Inc. network in the United States. In addition, beginning in 1987, several British financial institutions will join Plus under Royal Bank sponsorship and the network will also extend to Japan.

To help set itself apart in an industry where service is sometimes seen as undifferentiated and where "products" are copied relatively quickly, the Royal Bank provides many value-added services which have reinforced its reputation in the communities it serves. One example is *Your Money Matters,* a comprehensive consumer education program on personal and family money management. Encompassing mass-circulated self-help booklets, videos and branch staff workshops, the program has been extremely well received by employees, customers and the media.

The Bank also takes part in a variety of public relations, philanthropic and corporate sponsorship initiatives. Corporate donations and grants, in Canada and abroad, totalled $6 million in 1986. As an example, we sponsored the Canadian Junior Olympics for the 13th consecutive year. In addition, the Royal was co-sponsor of Vancouver's World Festival of the Performing Arts last summer, while the millions of visitors to Expo 86 in that city were able to do banking at on-site Royal Bank branches and banking machines. The Royal is official bank and Canadian distributor of ticket applications for the 1988 Winter Olympic Games in Calgary.

1

2

Tapping the experience and talents of retired Royal Bankers to market retirement investment products has been highly successful. The retirees, dubbed "Grey Panthers," are hired on a commission basis and trained in intensive 5-day sessions (1), such as the one led by instructor Peter Evans for a cross-country group of "recruits" to the program. Glen Anderson (2), who spent 37 years at the Royal, found the training invaluable for his sales calls on retired couples such as John and Martha Wettstein of Regina (seated). Anderson also works closely with Bank marketing manager Glenn Campbell and branch adminstration officer Linda Brady, who helps compile lists of prospective clients (3). Hiring pensioners to sell retirement products is unique in North American banking, earning the Royal a Golden Coin Award, top ranking among world banks for marketing programs in 1986.

1

Convenient access to banking service and target marketing at the grassroots are vital to meeting customer needs. In Halifax, a management team from our Atlantic field headquarters (1) plans service delivery through branches, Personal Touch Banking machines and commercial banking centres for a specific market area. They are (L-R): operations manager Ray Walker; network planner Ivan Greek; real estate manager Mike Byford; personnel specialist George Fancey; and retail banking vice president Les Pottie. Their planning efforts support thousands of customer service representatives, among them Paula Arsenault who explains Royal deposit options to a Halifax branch customer (3). Like many business people, Dr. K. S. Hoque (2, centre) is served both by his retail branch manager George Roberts (R) and commercial account manager Ken Gillis.

2

Independent Business

The Royal Bank serves 150,000 independent businesses, or one in four small firms in Canada. The Bank's strength in this rapidly-growing market rests on specialization in the products offered to entrepreneurs and in the way service is delivered.

During 1986, our loans and deposits both grew in this sector as established firms expanded and the number of new business starts continued at high levels. In recent years independent businesses have replaced large corporations as the most vigorous source of investment and employment growth. It is estimated that small firms now provide about 70% of new job creation and account for a significant share of new wealth generated in Canada.

3

The Royal was the first Canadian bank to recognize formally the unique needs of entrepreneurs by creating a separate management team for the independent business sector. This has helped us to respond more effectively than competitors to the needs of small firms. By concentrating account managers in strategically-located business units, the Bank is making their expertise more accessible to its clients—where they operate.

Many of our independent business account managers have received special training, including an intensive five-week classroom study course followed by up to a year of on-the-job instruction. The pace of these training programs has been accelerated in the year just completed.

Improvements in service accessibility and staff training are complemented by product innovation and enhancement in both deposit and credit services. All clients use our comprehensive range of deposit services, and many use a variety of fee-based services. For our 90,000 borrowing clients, the Bank offers a full range of credit services similar to those available to larger firms, including operating loans, fixed and floating rate term loans and commercial mortgages. Tailor-made programs are available for professionals such as doctors, lawyers and accountants, and a highly successful franchise-financing program serves this mushrooming market.

Because of the large number of new business starts in Canada, the independent business sector has received unprecedented attention from financial institutions. The Royal Bank's leading position—we have the largest market share—was achieved by responding to the special needs of small firms earlier and better than competitors. Our approach was and continues to be based on quick recognition of how an idea in the mind of an enterprising individual can bear fruit and grow into a significant business.

Agriculture

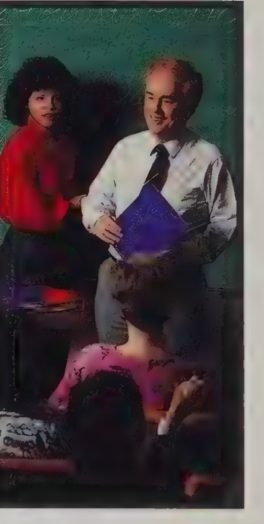
Agriculture in Canada experienced another difficult year during 1986, although there was improvement in certain sectors. High world grain inventories and the widespread recourse to export subsidies by the United States and the European Economic Community depressed selling prices. However, livestock and hog prices improved and show signs of continued strength.

Despite these adverse conditions, almost 95% of the Bank's farm loans remain current. During 1986, the Bank's 50 professional agrologists and other farm lending specialists worked diligently and effectively to support farmers. Every effort was made to keep farms in business, including renegotiations and the granting of additional loans wherever it was judged that an operation had a reasonable chance of survival. Most farm clients are capable managers, in many cases professionally trained. They are facing problems which were not foreseen when they assumed heavy debt loads to enter the business or to expand existing operations.

Because of the growing complexity of agricultural operations, the Bank has made significant investments in developing financial management tools for farmers. Our Farmchek cash flow monitoring system was upgraded in 1986 to allow participating farm clients to monitor monthly expenses and receipts. In addition, the Bank launched an enhanced computerized planning program, RoyFarm Financial Assistant, which helps our agrologists and branches in analyzing farm financial operations. Farmers who own personal computers may purchase this planning package from software retailers for their own use.

Government action in 1986 to establish farm debt review boards at the federal level and in some provinces injected a note of uncertainty into the Bank's operations in the agricultural sector. While a number of government initiatives in the past have been helpful, this new form of involvement limits our ability to protect Bank assets in cases where prudence dictates that foreclosure is the only appropriate course of action. This can only negatively influence Bank farm lending policy.

As the largest agricultural lender in Canada, the Bank is intimately familiar with and acutely aware of the problems facing farm producers and suppliers. We remain fully committed to the goal of building a stronger industry. Our efforts to keep farms operating under difficult economic conditions and to provide financial management tools for farmers offer ample evidence of that commitment.



More entrepreneurs count on the Royal than on any other bank in Canada. To meet their special needs, instructors like Dave Jenks and Anne Bourbonnière from our account management training centre regularly lead five-week courses to teach the fundamentals of serving independent business clients.

Commercial Banking

The Royal Bank offers business clients a broad array of financial products and services, delivered by professional commercial account managers attuned to the needs of corporate treasurers. Convenient access to service is also assured by our branch network, extensive electronic banking links and by our treasury, investment banking and international banking units across Canada and in major world financial centres.

In 1986, the Bank further strengthened its commercial product development and marketing programs, notably in the areas of electronic business banking and capital markets financing. Strong emphasis was also given to training programs designed to enhance the professional skills and knowledge of account managers.

This strategy was in tune with the commercial banking marketplace, where in 1986 the lack of growth in commercial credit demand worldwide further intensified competition. With the Canadian economy expanding at only a moderate pace, corporate treasurers continued to manage their debt loads very carefully and explore alternatives to bank lending, such as the longer term capital markets and commercial paper financing. In the energy sector, a steep decline in world oil prices had a severe impact, resulting in an increase in the Bank's commercial loan loss experience. Despite these conditions, the Royal Bank improved its overall market share of Canadian business credit, including bankers' acceptances.

Meanwhile, business demand for sophisticated treasury management services continued to grow rapidly. The Bank has correctly anticipated customer needs with products such as electronic cash management, payroll processing, capital markets financing, and foreign exchange and money markets services. In 1986, these services contributed substantially to the Bank's fee income, while helping businesses to optimize their resources and manage their financial affairs more effectively.

In commercial banking markets, as elsewhere, responsive sales and service is the key to competitive strength. This is the role of the Royal's account managers, our commercial sales force, who are primarily responsible for getting the Bank's extensive product offerings and resources working for clients in this sector.

Account managers need broad knowledge of a client's business, as well as of the Bank's capabilities and financial market trends. To enhance their knowledge, we have expanded our Professional Account Management Program, a training program focussing on new sales and relationship banking techniques.

Increasingly, account management teams are being assigned to specialized commercial centres, strategically located in key markets. By year end, the Bank had 20 commercial centres in 16 Canadian locations. While dealing with these centres, business clients also continue to maintain accounts and do day-to-day banking at the branches most convenient to them.

Once the groundwork is laid in class, on-the-job training in branches lasts up to a year. In Montreal, trainee Daniele Simard works with independent business account manager Pat Minicucci, himself a program graduate, honing the skills that will enable her to serve a growing small business sector.

Effective account management service to corporations depends on the availability of a broad line of banking products, many of which today go well beyond traditional banking frontiers. Electronic business banking is a prime example. Computer-based products such as CashCommand, PC CashCommand, Automated Payroll Service, PC Payroll and the LC Direct letter of credit service have made the Royal the leading ''electronic bank'' for Canadian business.

Many of these products are available to corporate and public sector treasurers via direct links with the Bank through their personal computers. Independent research indicates that by 1996 the desk-top computer may be as common in business offices as the telephone is today. We intend to plug our services into these high-tech work stations.

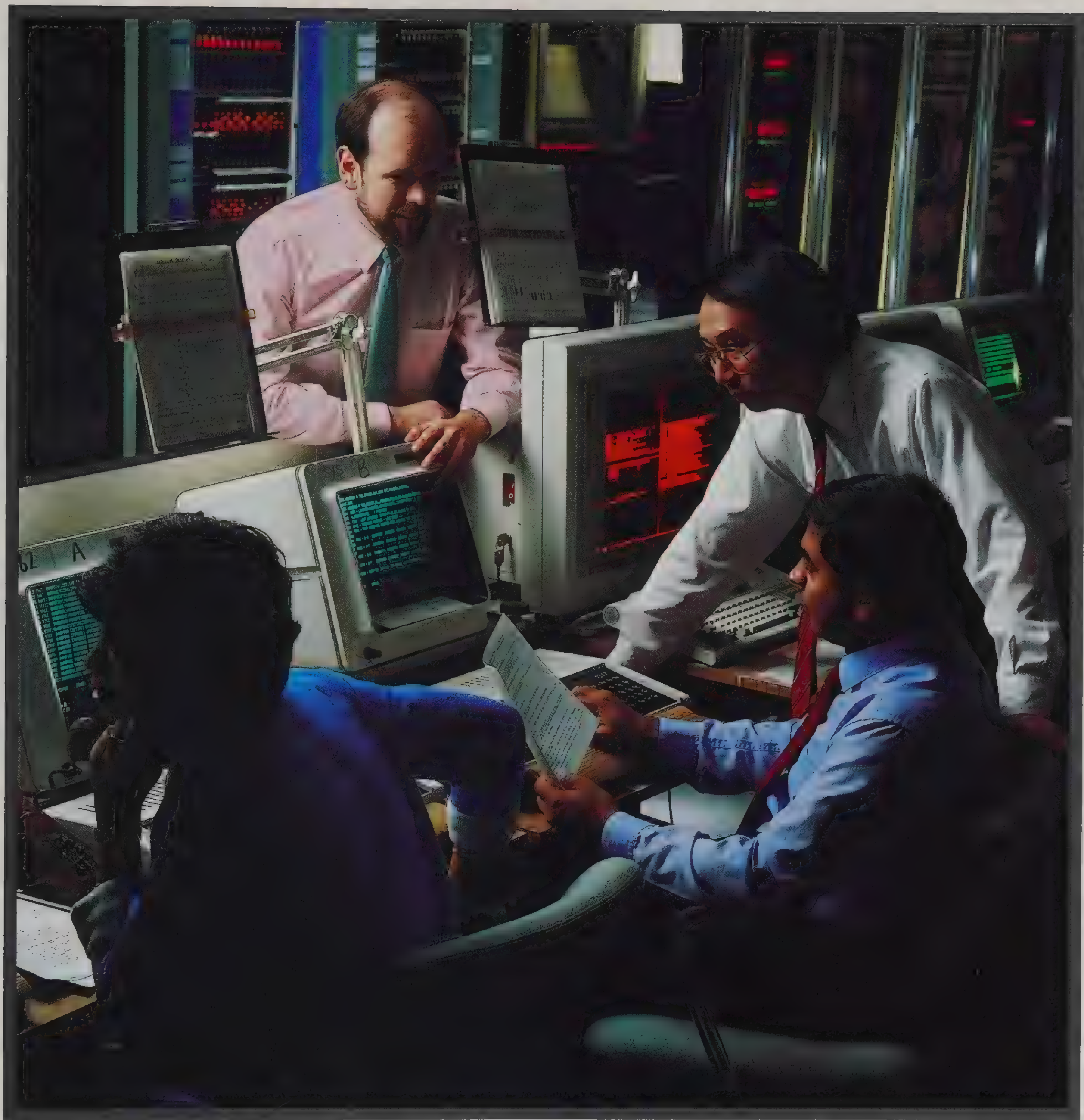
In addition to electronic cash management, the Royal leads in the market for automated payroll service, which was first introduced in 1968. We now prepare payroll for 10,000 Canadian businesses, placing us among the top four payroll service providers in North America.

Sometimes taken for granted in banking, information security is nevertheless emerging as a key feature of electronic treasury management services. For instance, customers have welcomed the new Royal Bank Security Card, a ''smart card'' incorporating a computer chip, which provides businesses with close control over access to microcomputer-based banking files.

The Royal continues to devise enhanced financing products for key market sectors. For example, FlexFinancing gives public sector treasurers the opportunity to raise short-term funds at competitive money-market rates, using a Royal Bank guarantee. This product is designed specifically for use by smaller public sector clients, such as municipalities, school boards and hospitals. Flex One-Million Plus gives larger borrowers access to a similar source of financing.

Business people look to the Royal for relevant economic, financial and treasury management information. We have responded with information services that include an extensive program of economic briefings for business people and two leading subscription publications—*Econoscope* and *Canadian Treasury Management Review.* To complement these and other services, the Bank has created a formalized education program, managed by our new Response Institute, which offers one-day seminars for business customers conducted by industry and bank experts.

3



1

2

To build on Royal Bank's lead in electronic business banking, commercial account managers marry knowledge of client needs with the skill of our technology experts. New York Life Insurance Company wants electronic banking services to "fit" its own state of the art information systems. Making that happen is a Bank team (1) including systems designers George Oliver (L), Alex Cheng and Sadru Teja (seated), at our communications network control centre in Toronto. They were mobilized by Royal account manager Dave Fardell (2), an insurance and institutional banking specialist. Fardell (R, standing) oversees banking arrangements with New York Life's treasury manager Joanne Petty, corporate vice-president finance David MacMahon (L, standing) and corporate vice-president information services David Rogers (R). Electronic links are reviewed (3) by Royal systems analyst Les Bell and Ian Tait (R), who heads New York Life's data control centre.

1

Large multinationals like Chrysler Corporation expect their top-tier banks to offer a complete range of credit, electronic and investment banking services. Managing our relationship with Chrysler requires teamwork by Royal Bankers in several countries. Here, U.S. relationship manager Ron Stanley (1, L) and his Canadian counterpart Doug Williamson (standing) discuss receivables financing with Fred Zuckerman, Chrysler's vice-president and treasurer, and Bob Baker, vice chairman of Chrysler Financial Corp (R). Investment banking advice comes from Nick Jordan (3) of Orion Royal Bank in London, which has been active in managing Euro-bond issues for the company. In Windsor, Ontario, Williamson is shown Chrysler Canada's high-tech van assembly line (2) by vice-president and treasurer Marty Welch (L). Together, they deal with a varied banking relationship, including treasury, payroll and branch service. The Royal is the company's lead Canadian bank.

2

Corporate/Investment Banking and Treasury

The nature of our business with large corporations and governments continued to change during 1986 as world financial markets evolved rapidly. We moved on multiple fronts to enhance our competitive position and long-term profitability.


3

Within the Bank, the most significant development was the introduction at mid-year of the revised corporate structure discussed earlier. The new Corporate/Investment Banking and Treasury Group emerged as a major element, with a global mandate to provide clients with a full range of financial services, including investment banking and treasury products. It accounts for approximately one-quarter of Bank assets and one-third of total deposits through three business units: Corporate and Government Banking; Investment Banking–North America and Treasury; Investment Banking–International. As other financial institutions are key clients for our extensive correspondent banking, treasury and investment banking services, we have placed our correspondent banking activity in the new group.

Considerable management attention was also devoted to the challenges presented by external market forces. The most dominant of these is the securitization of credit, which now involves the creation of tradeable financial instruments out of almost everything from corporate loans to consumer mortgages. Closely linked to securitization is the internationalization of world capital markets. Many of our customers now have global access to the capital markets, due to the breakdown of traditional local market barriers, the removal of foreign exchange controls and gains in communications technology. A third key trend is disintermediation. the by-product of securitization and the linkage of the international capital markets. Conventional corporate loans are less in demand as borrowers seek–and find–finer pricing via securitized loans.

These powerful trends–securitization, internationalization and disintermediation–are accelerating the pace of deregulation in some markets. The United Kingdom, for example, is the most deregulated major financial centre in the world. In Canada, deregulation is still lagging behind the market, although there were encouraging signs at the end of the year that regulatory change would quicken in 1987, particularly with respect to investment banking and securities trading.

Deregulation of financial markets was epitomized by London's "Big Bang" which, in October, radically altered the traditional pattern of trading securities on the London Stock Exchange. Orion Royal Bank Limited, our wholly-owned investment banking subsidiary, having acquired the London stockbroker Kitcat & Aitken earlier in the year, was well positioned among a select group of financial institutions to capitalize on these developments as a primary dealer in U.K. government securities, or "gilts." To handle this business, a new subsidiary, RBC Gilts, was formed. Kitcat & Aitken also plays a strategic role in the Bank's response to rapid internationalization of equity markets.

The nagging problem of third world debt, which has affected international banks for the past four years, is another environmental factor of concern, particularly considering the effects of oil price changes. However, after three years of austerity, many debtor countries have succeeded in making painful but necessary economic adjustments, improving their ability to repay interest on existing debt. At the end of the year, most of the Bank's loans to developing countries were current.

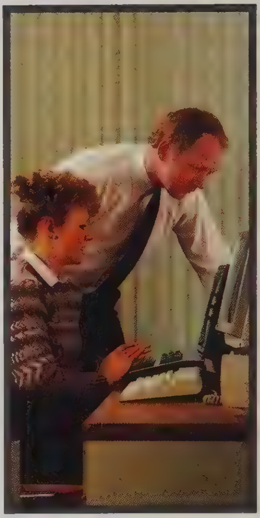
The mandate of our World Corporate Banking group was expanded in June to include service to governments. The new unit, Corporate and Government Banking, is a leader in the corporate market in Canada. Much of this business involves Canadian subsidiaries of foreign multinational corporations. As an example, our recently established ''Japan desk'' is developing business with the North American subsidiaries of Japanese companies and thus providing a ''springboard''—based on performance—for building relationships with parent companies in Japan. This was one of a number of initiatives designed to strengthen the Royal Bank Group's position in the important Japanese market.

The Japan desk is an extension of the relationship management concept, now widely adopted throughout the Bank. In the corporate sector, where competition continues to be intense, relationship management provides a needed edge. Our experience in the past five years clearly indicates that precise understanding of the customer's business and familiarity with the markets served is critical in the increasingly sophisticated corporate and institutional marketplace.

Relationship management fosters this kind of knowledge and understanding. Its successful application requires the ability to focus a bewildering array of corporate financial services and investment banking products on specific client needs. To this end, we continue to place considerable emphasis on training corporate bankers with such programs as our Corporate Financial Services workshop—an intense study program designed to upgrade product knowledge and focus on the newer capital market products.

Electronic banking is one of the main ''product lines'' offered by our relationship managers. Technology plays a critical role in the global reach of our corporate financial services, linking the Bank to clients through such services as RoyalCommand. This newly developed international cash management system allows treasury managers to analyze and manage the collection, concentration, disbursement and investment of the corporation's funds on a global basis.

Another feature of the corporate sector is that, increasingly, large corporations are raising funds directly in the capital markets. While this has greatly reduced the demand for conventional bank credit and locked some banks out of the funding process, it also offers opportunities to those with competitive investment banking capabilities.



To move our clients' money around the globe, the Royal calls on a network of correspondent banks in nearly every country. Reinforcing links with correspondents are specialized account managers, such as Andrew Willis in London. He teams up with Royal treasury trader Therese Kelly to pinpoint money market and foreign exchange services that appeal to a European bank.

The Royal is moving aggressively to exploit these opportunities by building on a proven ability to originate new products which offer clients direct access to less costly funding in the money and securities markets. We are also improving our capacity to trade these new products in the large volumes necessary to price them competitively and still generate revenue. Our investment banking and treasury network, which now includes 15 units worldwide, is important to the marketing of securitized products to investors and to developing the market information, liquidity and placing power required to win business.

Pursuing all three components of the business—origination, trading and distribution—is essential to remaining competitive.

Correspondent banks also deal with the Royal because of our efficient back office. Quick, accurate processing is the business of Ontario international centre, where Beverley Brooks (R) and Myrtle Nobrega work with our automated payments system. The centre supports a multitude of client services, including trade finance and international money transfers.

The investment banking activities of the Royal Bank Group are managed from a North American headquarters in Toronto and an International headquarters in London. The major operating unit, Orion Royal Bank, is the largest Canadian-owned investment bank in London and it is from there that the Royal's investment banking activities outside North America are driven. John R. Sanders was named chairman and chief executive officer of Orion Royal in October. He brings considerable experience and an outstanding reputation in the capital markets to his new assignment, which includes responsibility for all investment banking activities of the Royal Bank Group outside North America.

Orion Royal Bank is noted for its strength in the international capital markets. During the year, it was in the management group for some 480 Eurobond issues with an aggregate nominal value of U.S. $66 billion. In the second half of the year volatile conditions in the market and intense competition forced issue yields to unprofitable levels, and Orion declined some co-management invitations. It did, however, maintain a leading position in the Euro-Australian dollar bond market and continued to play a major role in the Euro-Canadian dollar bond market.

In the spring of 1986, Orion Royal's acquisition of Kitcat & Aitken further expanded the Royal Bank's growing investment management strength outside Canada. Funds under management in London grew steadily through the year. A broad range of investment services, including a very successful funds management capability, are also provided through The Royal Bank of Canada (Channel Islands) Ltd. Our Geneva-based subsidiary, The Royal Bank of Canada (Suisse), provides access to the Swiss domestic bond market, portfolio management and other private banking services. Orion Royal Bank Equities of Canada Limited, of London, was formed during the year to provide offshore distribution to institutional investors with an appetite for Canadian equities. In Germany, The Royal Bank of Canada A.G. has joined the German Federal Syndicate thereby giving us an additional product, German domestic bonds.

In North America, Investment Banking and Treasury provides foreign exchange and money market services along with merger and acquisition, venture capital and corporate finance expertise. During the year, the group developed and introduced a number of new services. For example, a swaps and interest rate management team was formed to assist clients in managing their exposure to both interest rate and currency fluctuations. In just six months, it became the leading swap team in Canada. Another new trading service is provided by our recently established corporate money market desk which, in its first four months of operation, increased monthly trading volume by 25%. A priority is the development of a Canadian government bond underwriting, trading and distribution capability based in Toronto. The groundwork for this was completed during the second half of 1986.

The Royal is the number one bank for foreign exchange trading in Canada and ranks among the top five in the field in North America. From an operational base in Toronto, the Bank has developed a global foreign exchange and money market presence with sizable operations in a number of other locations including London, New York, Tokyo, Hong Kong, Singapore and San Francisco. In Toronto, our state-of-the-art trading room has 92 positions and handles foreign exchange transactions of close to $4 billion daily.


3

Along with foreign exchange, treasury services to Canadian clients include interbank and wholesale deposits, treasury bills, bankers' acceptances, gold and silver, notes and bonds. These operations make a major contribution to the Bank's overall earnings. To better serve Canadian clients, a network of seven regional treasury units was set up two years ago. This initiative has paid dividends, improving our share of this competitive market. As well, we have substantially expanded market-making activity in bankers' acceptances for institutional clients, and registered solid growth in the distribution of Canadian treasury bills to retail clients. Gold and silver trading was also active in 1986.

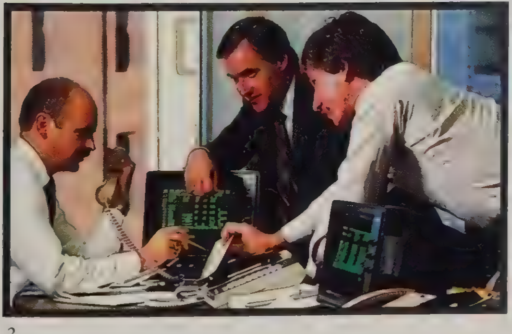
Our project finance team was involved in unique deals with the People's Republic of China during the year. Along with four other international banks, the Royal lead managed the first limited recourse financing for a Chinese enterprise, the Ping Shuo coal mine. The team also arranged a complex financing for the first investment in the North American market by China International Trust and Investment Company involving the purchase of a pulp mill in British Columbia.

International Network

In response to our growing emphasis on investment banking, improvements in communications systems and changes in Canada's trading patterns, the Bank has been streamlining its international banking network so as to better focus on client needs and profitable business opportunites.

The greatest change has taken place in the Caribbean and Latin America, where we have divested our operations in a number of countries over the past three years. These include: Guyana, Jamaica, St. Vincent, Haiti, and the Dominican Republic. At the same time, the Bank has strengthened its presence in such markets as Brazil, Puerto Rico,

1



2

As one of the top five North American banks in foreign exchange markets, the Royal offers clients 24-hour trading capability around the globe. In Toronto, each second counts for our traders, who handle nearly $4 billion a day in foreign exchange business (1). Sitting steps away, corporate dealer Cheryl Bell (3) markets the traders' services to large North American companies, giving them easy access to the leading edge financial markets savvy of our trading team. Trading activity also supports foreign exchange services in Royal branches and seven regional treasury service units across Canada. In Winnipeg (2), treasury services manager David Barsalou (R) closes deal for a business client of Norm Beaudry, commercial services manager (centre), while treasury officer George Dlugosh confirms rate over the phone.

Barbados and the Bahamas, where we have local commercial and retail banking operations that are both competitive and profitable.

During the past year, the Royal Bank also announced its intention to sell a small branch operation in Belize, as well as its 47% interest in The Royal Bank of Trinidad and Tobago Limited. As well, the Bank sold its 20% interest in Banco Royal Venezolano C.A. Our remaining business in Venezuela will continue to be facilitated from our representative office in Caracas. Finally, at year end, we also announced plans to close our single branch in Panama.

In Europe, the restructuring of our network included opening of an office in Milan. Also, we announced our intention to sell our wholly-owned U.K. retail banking subsidiary, Western Trust and Savings Limited.

In Asia, the Bank opened an office in New Delhi, reflecting the potential for increased trade flows between Canada and India. Our office in Bangkok, Thailand has been closed, with customers in that country being served through our off-shore banking units in Singapore and other Asia-Pacific locations.

In China, the Bank's presence was strengthened during the year by the growing activity of an office in Shenzhen, opened in late 1985, which works with our representative office in Beijing and a joint venture merchant bank in Hong Kong—China Investment and Finance Ltd.

In February 1986, we opened the doors of a new joint venture bank in Melbourne with our partners, The National Mutual Life Association of Australasia Limited. The new bank, National Mutual Royal Bank (NM Royal Bank) commenced operation with 46 retail branches. It also owns Capel Court, a leading Australian investment bank, which broadened operations in 1986 by acquiring 50% of the well-known stockbroking firm, T.C. Powell and Partners. Late in the year, after protracted negotiations, NM Royal Bank obtained approval to acquire the United Permanent Building Society with assets of A$1.5 billion and a network of 130 branches throughout the state of New South Wales. The merger will make NM Royal Bank the fifth largest bank in Australia with group assets of A$3.4 billion, a staff of 1800 and a network of 175 retail branches in the states of Victoria and New South Wales.

In most respects we have now developed the strategic geographic coverage required to meet the anticipated needs of our Canadian clients and other customers around the world.

Meeting those needs competitively is still largely a function of having the best people—the retail and commercial bankers, corporate finance specialists, investment bankers and the systems technicians and a host of others who work behind the scenes. This highly talented, professional group of bankers and ambassadors for Canada and the Royal Bank around the world represent an important competitive edge.

Client contact is the beginning and end of all Royal Bank team efforts. In Montreal, customer service representative Pauline Sènècal, putting a friendly face on Royal Bank service, sells British pounds to a travelling client. Branch foreign exchange service is supported, behind the scenes, by a trading team active in world money markets.

Management's Discussion of Financial Results:

This section of the Annual Report provides a comprehensive analysis of the Royal Bank's 1986 operating results as well as an explanation of how credit, liquidity, and interest rate risks are managed. Also included this year for the first time is a detailed discussion of the Bank's participation in the various instruments and services commonly referred to as "off-balance sheet activities".

For analytical purposes, the Bank divides its results into two geographic segments: Domestic and International operations. Domestic operations include all business transacted in Canada with the exception of the Canadian-based activities of the Bank's international money market units. Business carried on outside Canada, as well as the international money market function, comprise International operations.

In this segmentation of Domestic and International results, appropriate allocations have been made for corporate non-interest expenses and the cost of funds related to liquidity and capital.

CANADA'S ECONOMIC PERFORMANCE

The following analysis provides a perspective on Canada's economic performance between the third calendar quarters of 1985 and 1986. This period approximates the Bank's 1986 fiscal year.

Canada's economy continued to grow in fiscal 1986, but at a slower rate than that achieved during the previous few years. Real gross domestic product (GDP) advanced 3.5%, compared to an average 4.1% increase during the previous two years. However, much of the economic growth in fiscal 1986 reflected a strong surge in production at the beginning of the year.

Following that initial strength, the growth rate slowed significantly. In fact, the economy grew at an annual rate of only 1.2% during the July-September interval. Despite the slowdown in fiscal 1986, employment continued to rise at a respectable pace of 2.8%. This contributed to a further reduction in the jobless rate to 9.4% by the end of the year, almost one full percentage point below that of twelve months earlier. Inflation, as measured by the increase in consumer prices, remained stable near the 4% mark.

Slower economic growth in fiscal 1986 reflected a slight weakening in domestic demand and a significant reduction in net exports. On the domestic side, retail markets grew at a healthy pace in 1986, although not as quickly as in the preceding year. In real (inflation-adjusted) terms, consumer spending rose 4.4% during fiscal 1986, down from the 5.9% achieved during the previous four quarters. Much of this slowdown occurred in the category of durable goods, which registered real growth of 6.3%, compared to 14.7% a year earlier.

CHART 1
Real Economic Growth
(year-over-year % change in real GDP)

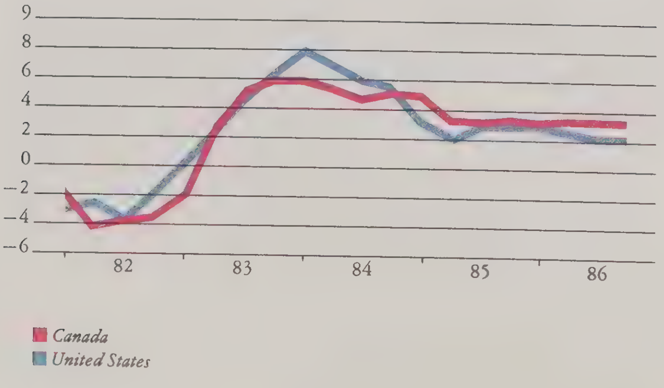
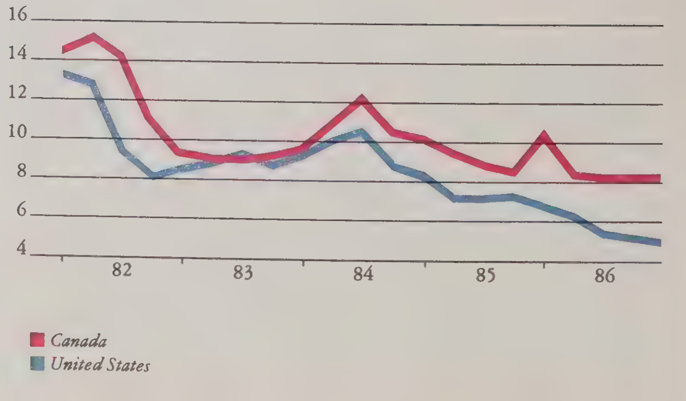


CHART 2
Interest Rates
(90-Day Treasury Bill Yields)
(Per Cent)



Weak business investment also contributed to slower economic growth in fiscal 1986. The long-awaited upturn in capital formation in 1985 was cut short by the sharp drop in world oil prices at the end of that year. During 1986, massive reductions in investment spending by the oil and gas industry offset very strong increases in manufacturing and moderate gains in other sectors. Total business outlays on plant and equipment dropped in real terms by 5.1%. Partly offsetting the weakness in non-residential investment, housing demand and construction boomed in 1986. Total housing starts jumped to 192,000 units, well up from 148,000 units in fiscal 1985.

Exacerbating the slowdown in domestic demand in fiscal 1986 was a significant deterioration in Canada's external trade performance. Sharply lower energy prices, weak commodity prices in general, and a decline in export volumes to the United States sliced Canada's merchandise trade surplus from $19.2 billion during 1985 to $11.0 billion in fiscal 1986. With respect to non-merchandise transactions, the external deficit widened to $19.8 billion from $18.5 billion during the previous year. Given these unfavourable movements in the trade of goods and services, the current account balance deteriorated to a deficit of $7.8 billion in fiscal 1986 from a surplus of $1.4 billion during the previous year.

The inter-related factors of weak commodity prices and deteriorating trade performance kept downward pressure on the value of the Canadian dollar for much of the year. In terms of U.S. dollars, the Canadian dollar fell from an average of 73.2 cents in October 1985 to 72 cents in October 1986. A relatively tight cash management policy by the Bank of Canada prevented an even larger decline in the dollar. Throughout the year, Canadian interest rate spreads with the United States were kept higher than usual. In fact, in February 1986 – a period of strong negative sentiment against the Canadian dollar – the 90-day treasury bill rate in Canada rose to an average of 11.6%, almost 4.5 percentage points above its U.S. counterpart. Following that period, the Canadian dollar became more stable, allowing the 90-day treasury bill rate to ease to 8.4% by the end of October.

Overview of 1986 Results

The effect of sharply lower world oil prices on energy sector borrowers combined with generally weak business loan demand placed considerable pressure on the Royal Bank's earnings in fiscal 1986. Despite encouraging results posted during the first six months, net income for the year of $489 million was virtually unchanged from the $488 million recorded in 1985. Basic earnings per common share declined to $4.05 from $4.28 last year, due to an increase in the average number of common shares outstanding from 97.3 million to 102.1 million. Earnings per share on a fully-diluted basis were $3.74 compared to $3.91 a year ago. This figure takes into account the number of common shares that would be issued upon conversion of certain debentures and preferred shares, as well as by the exercise of warrants.

The Bank's return on assets (ROA), one of the industry's most important measures of profitability, was .50%, slightly below last year's .53%. The Bank's ROA is composed of a Domestic ROA of .56% (.56% in 1985) and an International ROA of .38% (.47% in 1985). The return on common shareholders' equity was 12.0%, down from the previous year's figure of 13.5%.

At October 31, 1986, total assets had reached $99.6 billion, an increase of $3.6 billion or 4% over last year. Several factors contributed to the rise in assets, the most important being the healthy increase registered in mortgages and consumer instalment loans. At year end, these two categories accounted for $13.6 billion and $6.3 billion in outstanding balances respectively, up $2.5 billion and $500 million over the previous year. Mortgage lending was particularly strong during 1986, reflecting higher overall market activity and an increase in the Bank's market share. In addition, an increase in the value of several major foreign currencies vis-à-vis the Canadian dollar during fiscal 1986 resulted in an increase of roughly $1 billion in the translated value of the Bank's foreign currency-denominated assets. Continued weakness in the area of corporate lending resulted in an increase of only $800 million in Domestic business loans. Bankers' acceptances increased by a significant $1.3 billion as many corporate borrowers switched to this alternative method of financing.

Partially offsetting these increases was a decline of $2.2 billion in International loans to corporate and government borrowers, and a reduction of $500 million in the Bank's holding of Government of Canada securities.

Chart 3
Net Income
($ Millions)

The Royal Bank's asset mix has changed noticeably in recent years as consumer lending has taken on greater importance. At year-end 1986, consumer credit, including residential mortgages and consumer instalment loans, accounted for almost 30% of the Bank's total loans compared to roughly 22% four years ago. This segment, which is generally broadly diversified and of a low risk nature, has grown at an 11% compound annual rate since 1982.

At October 31, 1986, total capital funds, which include shareholders' equity, appropriations for contingencies, and bank debentures, stood at $6.7 billion, an increase of approximately $800 million or 14% over 1985. This increase consisted of approximately $100 million from the retention of current earnings and $800 million from new capital issues, including $129 million from the issue of shares under the Bank's Shareholder Dividend and Share Purchase Plan. This was partially offset by the repayment of $100 million in matured debentures.

The increase in capital along with limited asset growth brought about a further improvement in all of the Bank's capital ratios. At October 31, 1986, base capital, base capital equivalent, and adjusted total capital ratios, as defined by the Canadian regulatory authority were 4.2%, 4.7%, and 5.8% respectively, compared with 3.7%, 4.2%, and 5.3% at year-end 1985. A more detailed discussion of the Bank's capital position and ratios is found on page 48.

Domestic Operations

Since Domestic operations comprise roughly two-thirds of consolidated Bank assets, it is evident that the Bank's financial performance is strongly influenced by the health of the Canadian economy. Economic growth was uneven throughout 1986, reflecting the difficult conditions prevailing in Canada's resource-based industries, most particularly in the oil and gas sector. These events coupled with the continued shift toward non-bank sources of credit by large commercial and corporate borrowers significantly constrained business loan growth in fiscal 1986.

Weakness in the corporate lending market, however, was more than offset by excellent results in retail banking, where demand for mortgages and consumer loans was strong. While competition for new mortgage business remained intense, the Royal Bank improved its market share in this category.

For the year just ended, earnings from Domestic operations totalled $361 million, representing an increase of 9% over 1985. Return on assets of .56% remained unchanged from a year ago.

In 1986, average total Domestic assets were $64.0 billion, rising $5.2 billion or 9% from last year. The Bank's Domestic net interest margin improved moderately from 1985, rising 16 basis points to 3.43%.

Other income from Domestic operations rose $76 million or 13% from the previous year, reflecting increases in service charge revenues and higher credit card transaction volumes.

Chart 4
Average Total Assets
($ Billions)

Chart 5
Consumer Loan Business
(% of Average Total Loans)

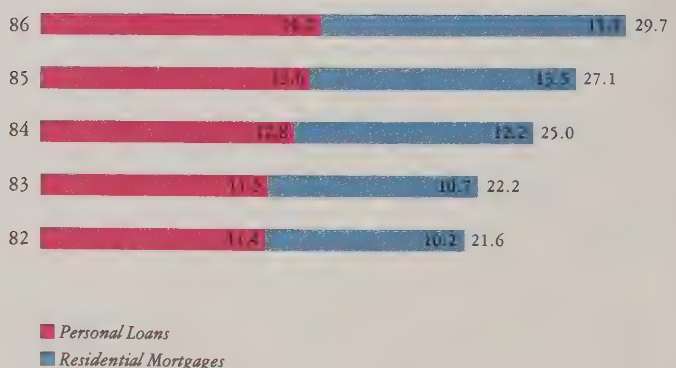


Table 1

HIGHLIGHTS OF DOMESTIC EARNINGS
(as a per cent of average assets)

	1986	*1985*	*1984*	*1983*	*1982*
Net interest income (taxable equivalent basis)	**3.43%**	3.27%	3.49%	3.41%	2.67%
Provision for loan losses	**(.70)**	(.58)	(.59)	(.55)	(.46)
	2.73	2.69	2.90	2.86	2.21
Other income	**1.03**	.99	.96	.86	.71
	3.76	3.68	3.86	3.72	2.92
Non-interest expenses	**(2.63)**	(2.60)	(2.58)	(2.44)	(2.33)
	1.13	1.08	1.28	1.28	.59
Income taxes (including taxable equivalent adjustment)	**(.57)**	(.52)	(.63)	(.62)	(.30)
Return on assets	**.56%**	.56%	.65%	.66%	.29%
Net income ($ millions)	**$ 361**	$ 331	$ 359	$ 374	$ 162
Average assets ($ billions)	**$64.0**	$58.8	$55.3	$56.6	$56.0

Domestic non-interest expenses – consisting of salaries and employee benefits, property costs, computer and telecommunications expenses, and other costs of doing business – grew by 10% in 1986. This rate of growth, which is significantly higher than a year ago, reflects sharply higher deposit insurance premiums (up $17 million or 155%) as well as increased business and federal and provincial capital taxes (up $39 million or 76%). Operating expenses were also affected by higher technology-related expenditures, which reflect the Bank's commitment to improving efficiency through automation.

In 1986, Domestic loan loss experience rose by almost $200 million to $540 million as a direct consequence of the serious problems affecting the oil and gas sector in western Canada. The charge to Domestic earnings (the provision for loan losses) amounted to $445 million in 1986, an increase of $102 million or 30% from a year ago. At October 31, 1986, Domestic non-accrual loans, net of provisions for losses, were $1.6 billion, an increase of approximately $340 million over the previous year end. The net yield on this portfolio declined from 2.2% to 1.0%.

CHART 6
Return on Assets
(% of Average Assets)

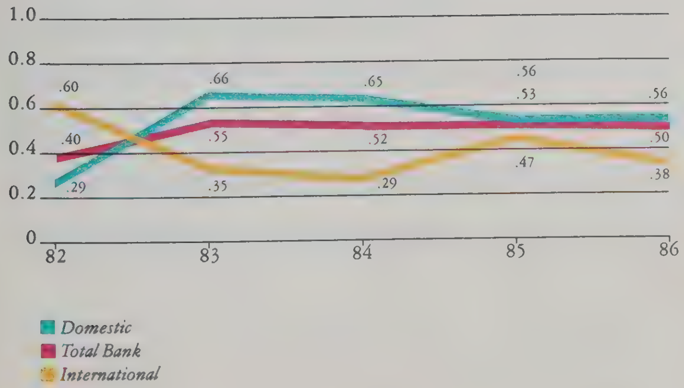


CHART 7
Return on Equity
(Per Cent)

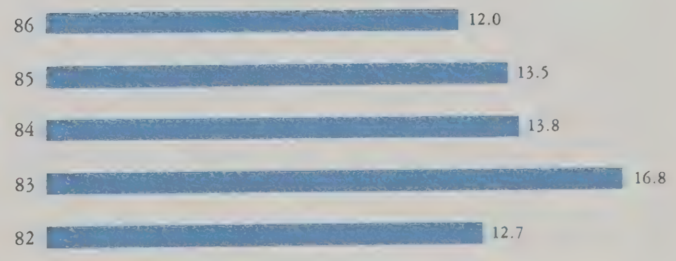


Table 2

HIGHLIGHTS OF INTERNATIONAL EARNINGS

(as a per cent of average assets)

	1986	*1985*	*1984*	*1983*	*1982*
Net interest income (taxable equivalent basis)	2.18%	2.06%	1.73%	1.65%	1.85%
Provision for loan losses	(1.10)	(.83)	(.66)	(.47)	(.26)
	1.08	1.23	1.07	1.18	1.59
Other income	.72	.70	.56	.59	.57
	1.80	1.93	1.63	1.77	2.16
Non-interest expenses	(1.45)	(1.25)	(1.20)	(1.19)	(1.13)
	.35	.68	.43	.58	1.03
Income taxes (including taxable equivalent adjustment)	.03	(.21)	(.14)	(.23)	(.43)
Return on assets	.38%	.47%	.29%	.35%	.60%
Net income ($ millions)	$ 128	$ 157	$ 91	$ 106	$ 196
Average assets ($ billions)	$33.7	$33.5	$31.4	$30.1	$32.5

INTERNATIONAL OPERATIONS

An increase in the provision for loan losses and volatile conditions in global credit and capital markets resulted in lower earnings for the Bank's International operations in fiscal 1986. International net income was $128 million, declining $29 million from last year. At .38%, return on assets was 9 basis points lower than the .47% reported in 1985 but still 9 basis points above the 1984 level.

On the positive side, International net interest income rose by 6% during the year, reaching $734 million. This increase in revenue stemmed mainly from an improvement in the International non-performing loan portfolio, where the level of net non-accrual loans fell from $1.2 billion to $700 million during fiscal 1986. This reduction was primarily due to the return to current status of loans to Argentina and the Dominican Republic, and to the increase in the level of specific and general provisions maintained for International loans.

International loan loss experience increased in 1986, rising from $340 million to $435 million, due in large part to an increase in the amount added to the Bank's general provision for lending to 32 financially troubled countries specified by the Office of the Inspector General of Banks. The 1986 addition to the general provision was $265 million, raising the cumulative amount to $628 million or approximately 11% of the Bank's aggregate exposure to these countries. The provision for loan losses used in determining International earnings increased by 34% to $372 million.

Other income rose $10 million internationally, reaching $244 million. Solid growth in revenues from foreign exchange trading outweighed a decline in fees from securities underwriting.

A concerted effort was made in 1986 to strengthen the Bank's position in the increasingly competitive area of investment banking. This strategy was pursued most actively in the United Kingdom in preparation for the opportunities provided by the deregulation of London's capital markets in October 1986. The two most significant initiatives were the acquisition of the remaining 70% of Kitcat & Aitken, the London stockbroker, which gave the Bank a presence in the British equities market, and the establishment of RBC Gilts. This government bond trading subsidiary allowed the Royal Bank to become the only Canadian bank licensed as a primary dealer in the rapidly-expanding U.K. government securities market.

International non-interest expenses totalled $487 million in 1986, an increase of $68 million over the prior year. Of this increase, approximately $23 million was due to the translation effect of a weaker Canadian dollar while $10 million was due to the strategic initiatives described above. Excluding these factors, operating costs rose by 8% in 1986.

Selective rationalization of the Bank's International network continued in 1986. In an effort to employ resources more productively, the Bank sold its branch operations in Haiti, closed its representative office in Thailand, and opened representative offices in India and Italy.

Table 3

Analysis of Changes in Net Interest Income
($ Millions)

	1986 vs 1985			1985 vs 1984		
	Increase (decrease) due to changes in			*Increase (decrease) due to changes in*		
	Average Volume(1)	*Average Rate(1)*	*Net Change*	*Average Volume(1)*	*Average Rate(1)*	*Net Change*
Assets						
Deposits with other banks	$ (98)	$(179)	$(277)	$135	$ (31)	$104
Securities						
Loan substitutes	(30)	(5)	(35)	(12)	(57)	(69)
Other securities	204	(85)	119	128	(52)	76
Loans						
Domestic						
Mortgages and consumer instalment loans	277	(127)	150	221	(16)	205
Other loans	129	(154)	(25)	60	(195)	(135)
International						
Mortgages and consumer instalment loans	47	(4)	43	(3)	4	1
Other loans	(2)	(227)	(229)	77	(132)	(55)
Total interest income	527	(781)	(254)	606	(479)	127
Liabilities						
Deposits						
Domestic						
Demand	4	(14)	(10)	(9)	(33)	(42)
Notice	137	(26)	111	164	(103)	61
Fixed-term	127	(191)	(64)	20	(23)	(3)
International						
Demand	2	5	7	1	(14)	(13)
Notice	22	(15)	7	4	(19)	(15)
Fixed-term	(93)	(545)	(638)	197	(227)	(30)
Debentures and other liabilities	47	(24)	23	34	(6)	28
Total interest expense	246	(810)	(564)	411	(425)	(14)
Net Interest Income	$281	$ 29	$310	$195	$ (54)	$141

(1) Rate/Volume variance is allocated based on the percentage relationship of changes in volume and changes in rate to the total net change.

Net Interest Income

Net interest income is the principal source of revenue for banks. It is the difference between interest earned on loans and securities, and interest paid on deposits and debentures. For analytical purposes, net interest income is adjusted to take into account the tax-exempt status in Canada of income from certain securities, primarily ''loan substitute'' securities such as term preferred shares, income debentures and small business bonds. (For a more detailed discussion of the effects of tax-exempt income, see Income Taxes, page 42). Including this taxable equivalent adjustment of $174 million, net interest income for 1986 totalled $2.9 billion, more than $300 million above last year's figure.

Chart 8
Net Interest Income
($ Millions)

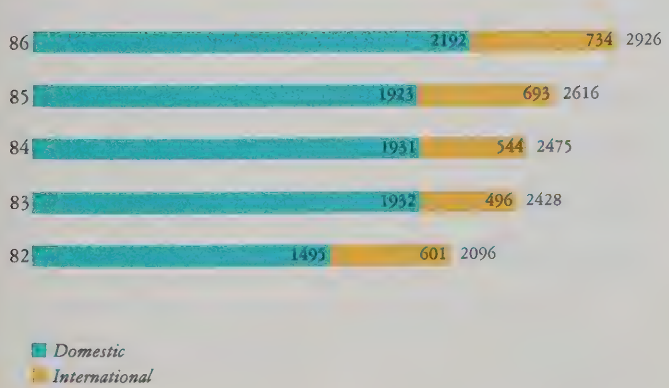


Chart 9
Net Interest Margin
(% of Average Assets)

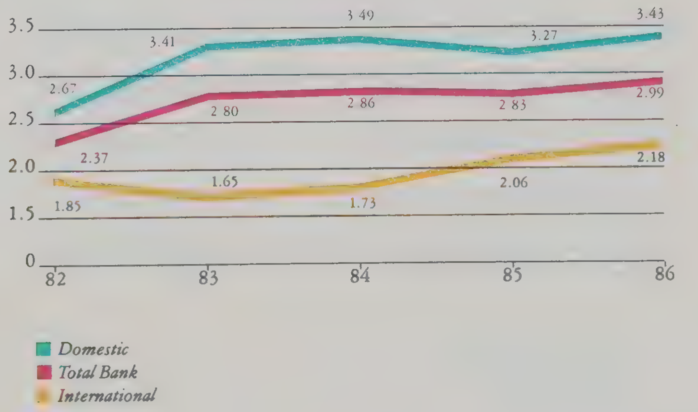


Table 4

NET GAINS (LOSSES) ON DISPOSAL OF SECURITIES
($ Millions)

	1986	*1985*	*1984*	*1983*	*1982*
Equity securities	$ 90	$34	$31	$49	$15
Debt securities (1)	15	(5)	(17)	(22)	(24)
Total	$105	$29	$14	$27	$(9)

(1) Gains (losses) on disposal of debt securities represent the portion of gains and losses amortized to income in the year indicated.

Two key factors determine the Bank's net interest income: the net interest margin, which is the percentage spread the Bank earns on its assets after accounting for the cost of deposits; and the change in the volume of average earning assets. A volume/rate analysis of the changes in net interest income over the past two years is shown in Table 3. Pages 54 and 55, in the Supplementary Financial Review section, present a three-year average balance sheet showing the respective yields and costs of individual asset and liability components.

In 1986, $281 million of the growth in net interest income was attributable to a 5% increase in average earning assets. Performance was further enhanced by higher overall margins, which accounted for an additional $29 million gain. Net interest income expressed as a percentage of average total assets (net interest margin or "spread") climbed 16 basis points above last year's level, reaching 2.99%. The overall yield on assets declined by 82 basis points while the average cost of funds fell more rapidly, dropping 98 basis points. Chart 9 illustrates Domestic and International net interest margins for the past five years. As the chart reveals, the significant retail component of Domestic operations has traditionally resulted in a significantly higher margin than for International operations, where lending is predominantly of a wholesale nature. In 1986 the Domestic margin rose 16 basis points while the International margin climbed by 12 basis points, reaching 3.43% and 2.18% respectively.

The increase in Domestic spread over last year is explained by several factors. First, growth in the Bank's Domestic loan portfolio was concentrated in higher yielding categories, most notably mortgages and consumer instalment loans. Second, during the year, clients demonstrated a preference for longer loan maturities (at a higher yield to the Bank) and shorter deposit maturities (at a lower cost to the Bank). Consequently, the average cost of funds declined more rapidly than the yield on assets. Also, sharply higher levels of both equity and bond gains were attained in 1986, but these were partially offset by lower yields on non-accrual loans.

The mix and relative costs of the Bank's various deposit sources are also fundamental determinants of net interest income. A breakdown of total Domestic deposits, amounting to $51.5 billion, is provided in Chart 11. Notice deposits were higher this year, while demand deposit and higher-cost term deposit balances were largely unchanged. At year end, Domestic consumer deposits totalled $37.0 billion, $2.1 billion or 6% higher than 1985, and currently represent over 70% of Domestic deposits. These stable core deposits, which permit less reliance on higher cost and more volatile sources of funds, remain one of the Royal Bank's most important strengths.

Internationally, the net interest margin also improved from 1985, approaching the peak level reached in 1981. A decline in International non-accrual loan balances combined with lower interest rates caused a significant reduction in the cost of carrying problem loans. This was the principal reason for the improvement in the International net interest margin.

CHART 10
Global Deposit Mix (as at October 31)
(% of Total Deposits)

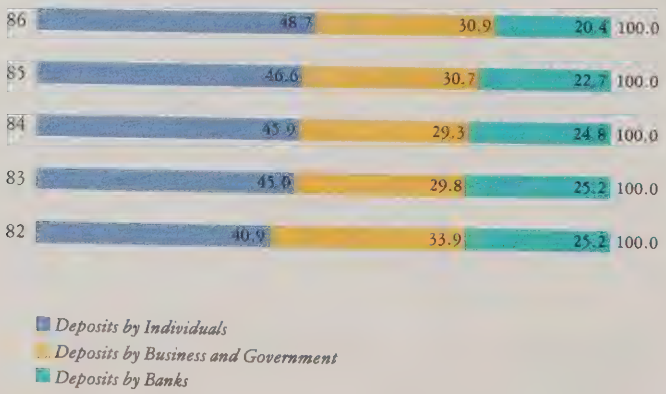
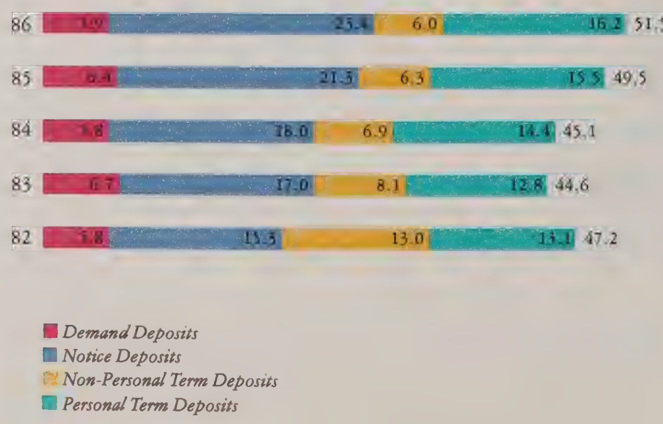


CHART 11
Domestic Deposits (as at October 31)
($ Billions)



For the Bank as a whole, the net interest yield on non-accrual loans (the difference between total interest received on existing net non-accrual loans and interest reversed on newly classified loans) was approximately 4.2% on an average balance of $2.1 billion. Table 6 segments this yield into its Domestic and International components which, for 1986, were 1.0% and 9.6% respectively. In addition, the Bank had an average balance of renegotiated reduced-rate loans of $140 million in 1986 which generated a yield of 6.7%.

The Bank manages, for its own account, an investment portfolio of debt and equity securities. Table 4 presents a five-year summary of net gains and losses on the disposal of these securities. For accounting purposes, gains and losses on the sale of equity securities are recorded in the period in which they occur while realized bond gains and losses are amortized to earnings over a five-year period. During 1986, bond prices generally rose in reaction to lower interest rates. Equity markets were somewhat unstable, reflecting the prevailing uncertainty regarding energy prices and interest rates. Full-year taxable equivalent equity gains, which were registered largely in the first half of fiscal 1986, were $90 million, while amortized bond gains totalled $15 million. The Bank's net gain on the disposal of securities was $105 million compared with $29 million in 1985. These securities gains were offset to an extent by sharply lower income from equity accounted investments and money market trading activities. In addition, it should be noted that the Bank currently has $66 million of realized but deferred bond gains, which will be taken into earnings in the periods ahead.

Non-Performing Loans and Loan Losses

Non-Performing Loans

Since the worldwide recession of the early 1980s, non-performing loans and related loan losses have been the most serious barriers to the Bank's progress in attaining higher levels of profitability. Although the economic recovery and lower interest rates in recent years have helped many financially troubled borrowers, certain industries – particularly those in the resource sector – have not shared fully in the turnaround. The sharp drop in 1986 in world oil prices left companies in the oil and gas sector with severe cash flow problems and, in some cases, with an inability to fully service debt obligations. As well, many country borrowers, particularly in Latin America, remain burdened by heavy debt-servicing commitments and depressed prices for export commodities.

For analytical purposes, there are two separate categories of non-performing loans – non-accrual loans and renegotiated reduced-rate loans. Non-accrual loans are those loans which have been placed on a cash basis because management feels that the collectibility of principal or interest is in doubt. Loans are automatically placed on a cash basis (interest income is recognized only when cash is received) when payment of interest is ninety days past due, except in certain rare cases where management has determined that the collectibility of principal and interest is not in doubt.

When a loan is placed on a non-accrual basis, there may be accrued interest which had been recognized as income but not yet received in cash. This unpaid interest is reversed, or deducted from income. Subsequent interest received on a non-accrual loan is recorded as income only if management has determined that the loan does not require a specific provision for loss; otherwise, interest received is credited to the principal amount of the loan. Non-accrual loans are restored to an accrual basis when principal and interest payments are current and there is no longer any reasonable doubt regarding collectibility.

Renegotiated reduced-rate loans are those loans which, due to a deterioration in the financial position of the borrower, have been renegotiated to provide for a rate of interest lower than the prevailing market rates on similar loans to new borrowers.

During 1986, the Bank's level of total non-accrual loans, net of provisions for losses, fell to $2.3 billion, declining for the third consecutive year. As Table 5 illustrates, the substantial drop in International non-accrual loan balances more than compensated for the considerable increase reported in Domestic operations.

At year-end 1986, the Bank's Domestic net non-accrual loans totalled $1.6 billion, an increase of $336 million over 1985. As mentioned earlier, this is a consequence of lower energy prices. Non-accrual loans to Domestic borrowers in the energy field amounted to approximately $800 million at October 31, 1986. Renegotiated reduced-rate loans, virtually all of which were Domestic, amounted to $77 million, falling $103 million from the end of 1985.

In International operations, net non-accrual loans fell from $1.2 billion at year-end 1985 to $726 million this year. This improvement arises from the reclassification to performing status of loans to Argentina and to the Dominican Republic, and to higher specific and general provisions maintained against International loans outstanding. Of the balance of non-accrual loans, approximately half are to borrowers in the United States, and of this amount, roughly three-quarters are to customers in the energy and real estate industries.

As indicated in the section on Net Interest Income (page 35), the overall yield generated by non-accrual loans this year was approximately 4.2%, down from 5.6% in 1985.

Loan Losses

Loan loss experience represents the Bank's best estimate of the additional specific and general provisions required to cover potential losses in its loan portfolio. Specific provisions are established on a loan-by-loan basis to recognize anticipated losses on identified problem loans. General provisions are made against the Bank's aggregate exposure to the 32 troubled countries identified by the Office of the Inspector General of Banks. Accumulated specific and general provisions are deducted in determining the loan balances shown on the balance sheet.

Loan loss experience for a given year is equal to the current year's loan write-offs, net of recoveries, plus the year-over-year change in accumulated specific and general provisions for losses carried on the balance sheet. The portion of the loan loss experience charged to income (called the provision for loan losses) is based on a formula prescribed by the Canadian regulatory authority, which has the effect of averaging the loan loss experience over a five-year period. Any difference between the loan loss experience and the provision for loan losses is charged or credited directly to capital.

The Royal Bank's loan loss experience rose by $290 million during 1986 to $975 million. Table 7 provides a geographic breakdown of loan losses over the past five years, and highlights that most of the large increase this year is attributable to Domestic operations.

Table 5

NON-PERFORMING LOANS *(net of provisions for losses)*

As at October 31
($ Millions)

	1986	1985	1984	1983	1982
Non-accrual Loans					
Domestic					
Atlantic Provinces	$ 9	$ 7	$ 9	$ 13	$ 30
Quebec	89	115	90	87	53
Ontario	83	107	126	145	155
Manitoba	36	36	39	42	49
Saskatchewan	100	72	54	37	19
Alberta	960	376	567	681	577
British Columbia	290	518	522	627	369
	1,567	1,231	1,407	1,632	1,252
Of which:					
Consumer instalment, mortgages and other personal loans	56	55	77	133	174
Agriculture and independent business	268	289	279	255	231
Large commercial and corporate	1,243	887	1,051	1,244	847
	1,567	1,231	1,407	1,632	1,252
International (1)					
U.S.A.	369	373	277	464	183
Europe, Middle East and Africa	233	127	127	216	140
Latin America and Caribbean	52	680	832	486	460
Asia Pacific	72	38	40	40	5
	726	1,218	1,276	1,206	788
Total	$2,293	$2,449	$2,683	$2,838	$2,040
Renegotiated Reduced-Rate Loans					
Domestic	$71	$175	$106	N/A	N/A
International	6	5	—	N/A	N/A
Total	$77	$180	$106	N/A	N/A

(1) Net of a general provision for losses on country lending which has been allocated to the appropriate areas based on relative balances outstanding to problem countries.

Domestic loan loss experience of $540 million was $195 million higher than in 1985. This increase is due to the difficulties experienced by borrowers in the resource sector of western Canada. Of the Bank's total Domestic loss experience in 1986, $225 million represented losses related to the energy sector.

Internationally, loan losses amounted to $435 million in 1986, $95 million higher than 1985. This increase is attributable partly to losses on loans to private sector borrowers in the oil and gas industry, which accounted for $100 million of loan losses in 1986, as well as to a year-over-year increase in the general provision for country lending. In view of the problems experienced by a number of countries in servicing their external financial obligations, the Bank began to build up a general provision for its aggregate cross-border lending to such countries in 1983. In fiscal 1986, the Bank added $265 million to its general provision, bringing the aggregate total to $628 million or approximately 11% of outstandings to these country borrowers.

Table 6

INTEREST EARNED ON NON-ACCRUAL LOANS (1)

(net of provisions for losses)
($ Millions)

	1986	1985
Domestic		
Average balances	$1,347	$1,389
Interest earned	$14	$30
% Yield	1.0%	2.2%
International		
Average balances	$800	$1,298
Interest earned	$77	$121
% Yield	9.6%	9.3%
Total		
Average balances	$2,147	$2,687
Interest earned	$91	$151
% Yield	4.2%	5.6%

(1) Interest earned on non-accrual loans comprises interest received on non-accrual loans net of interest reversals on newly-classified loans.

Table 7

DETAIL OF LOAN LOSSES
($ Millions)

	1986	1985	1984	1983	1982
Loan Loss Experience					
Domestic					
Atlantic Provinces	$ 9	$ 6	$ 2	$ —	$ 18
Quebec	33	22	18	48	54
Ontario	52	38	26	78	63
Manitoba	16	11	17	14	16
Saskatchewan	27	27	11	11	6
Alberta	327	152	202	229	257
British Columbia	76	89	104	74	116
	540	345	380	454	530
Of which:					
Consumer instalment, credit cards, mortgages and other personal loans	54	49	48	92	77
Agriculture and independent business	121	99	84	104	84
Large commercial and corporate	365	197	248	258	369
	540	345	380	454	530
International (1)					
U.S.A.	115	83	169	174	75
Europe, Middle East and Africa	(10)	39	48	85	57
Latin America and Caribbean	304	198	123	45	18
Asia Pacific	26	20	22	14	—
	435	340	362	318	150
Total	$975	$685	$742	$772	$680
Eligible Loans					
Domestic	$51,104	$46,184	$45,476	$44,726	$47,178
International	22,486	22,850	21,281	20,529	20,904
Total	$73,590	$69,034	$66,757	$65,255	$68,082
Loss Experience as a Per Cent of Eligible Loans					
Domestic	1.06%	.75%	.84%	1.01%	1.12%
International	1.93	1.49	1.70	1.55	.72
Total	1.32%	.99%	1.11%	1.18%	1.00%
Provision for Loan Losses (five-year average)					
Domestic	$445	$343	$327	$309	$258
International	372	278	208	143	86
Total	$817	$621	$535	$452	$344

(1) Includes a general provision for losses on country lending which has been allocated to the appropriate areas based on relative balances outstanding to problem countries.

In the periods ahead, it is the Bank's intention to add to this general provision. This policy is similar to that of international banks in other jurisdictions and is consistent with the views of the Canadian regulatory authority. A detailed discussion of the international debt situation, including a review of the Bank's exposure to the major troubled borrower nations in Latin America, can be found on page 44 in the section on Portfolio Risk Management.

The provision for loan losses, which is the amount charged to income, was $817 million in 1986, up $196 million or 32% over last year. Within Domestic operations, this figure amounted to $445 million, up $102 million from 1985. The International provision for loan losses rose $94 million to $372 million.

Other Income

Although income from interest and dividends represents the cornerstone of the Bank's operating revenue, a sizeable and growing portion stems from a broad range of non-asset-based financial services. This fee-based or "other" income includes such items as credit card fees and commissions, service charges on deposit accounts, securities commissions, loan administration fees, foreign exchange trading profits, and fees from other non-interest sources. The Royal Bank continues to expand and diversify such revenue sources, particularly in the current environment of relatively slow asset growth and increasing use of capital market financing by corporate borrowers.

In 1986, other income remained strong, reaching $904 million, a 10% gain over last year. Table 8 shows other income for the past two years broken down into its principal components.

At $321 million, service charge income rose 13% during 1986, reflecting increased usage of retail and commercial deposit account services and selected price adjustments on these services.

Credit card fee income, including user-fees and merchant discount revenue from Visa and Diners Club, was up from $109 million in 1985 to $117 million this year, mainly due to higher transaction volumes.

Loan and commitment fee income rose 7% in 1986 to $101 million, mainly as a result of growth in Domestic operations.

Earnings from securities commissions increased 10% to $56 million. Despite reduced underwriting revenues in the Bank's investment banking operations, good performances were turned in by both Domestic and other areas of International operations.

This year saw healthy growth in foreign exchange revenues, with income rising from $134 million in 1985 to $150 million in 1986 – a growth rate of 12%. Volatility in currency markets during the year gave rise to many opportunities to generate earnings from foreign exchange transactions. The total value of such transactions reached $2.2 trillion, an indication of the Bank's strength in this important area.

Chart 12
Other Income
(% of Average Assets)

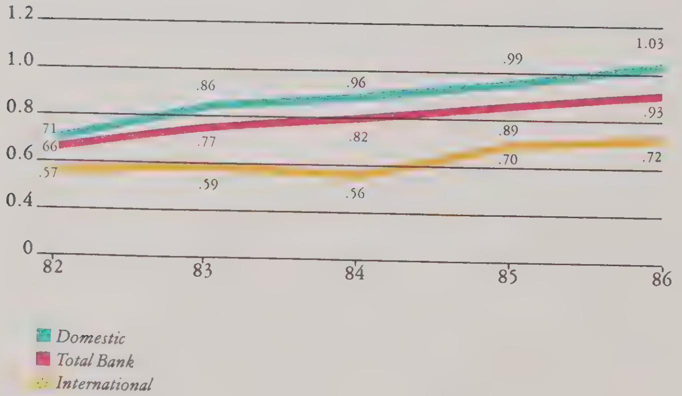


Table 8

Other Income
($ Millions)

	1986	*1985*	% *Change*
Service charges	**$321**	$284	13.0%
Foreign exchange revenue	**150**	134	11.9
Credit card fees	**117**	109	7.3
Loan and commitment fees	**101**	94	7.4
Bankers' acceptances, letters of credit and guarantee fees	**77**	72	6.9
Securities commissions	**56**	51	9.8
Other	**82**	74	10.8
Total	**$904**	$818	10.5%

Fees from bankers' acceptances, letters of credit and guarantees were $77 million, up $5 million or 7% from last year. This increase reflects the particularly strong growth in bankers' acceptances during 1986 due to more favourable pricing for business borrowers during the second half of the fiscal year.

Non-Interest Expenses

Non-interest expenses consist of all costs incurred in the Bank's operations with the exception of interest expense, the provision for loan losses, and income taxes. The Bank's primary operational goal is to provide the best possible service to its customers in the most cost-efficient manner. Being a customer-oriented business necessitates the employment of sufficient staff and up-to-date banking technology to meet client needs. Staff costs alone comprise almost 60% of the Bank's non-interest expenses. In 1986, non-interest expenses totalled almost $2.2 billion, up 11.5% from the 1985 level.

Staff costs, which include salaries, pensions, and other employee benefits, amounted to approximately $1.3 billion in 1986, an increase of 6% over 1985. Several factors contributed to this growth in staff-related expenses, including a general rise in compensation levels, an increase in total paid staff from 41,951 at the end of 1985 to 43,229 at year-end 1986, and outlays associated with the Bank's new employee share purchase plan, which was introduced in June 1985. Also, part of the increase in staff costs is associated with various investment banking initiatives undertaken in the U.K. in preparation for new opportunities arising from the deregulation of London's capital markets.

Partially offsetting this rise in staff costs was a reduction in the Bank's pension fund expense of approximately $14 million. This is due to a recent change in Canadian accounting guidelines which is more fully explained in Note 13 to the Financial Statements on page 70. This note also provides information on the funding excess of the Bank's pension plan, which stood at $226 million at January 1, 1986.

Additional cost reductions were derived from the continuing rationalization of the Bank's International network. Selective divestitures were made in 1986 to ensure that each operating unit enhances the Bank's strategic position in the highly competitive global market and contributes to the attainment of short and long-term financial goals.

The Royal Bank's commitment to remaining at the forefront of automated banking technology necessitates substantial capital spending on computers and other related equipment. While such capital outlays may reduce short-term profitability, they position the Bank to reap future benefits. Principally because of this expansion of the Bank's electronic network (which includes automated banking machines, computers, and related telecommunications equipment), premises and equipment costs rose 16% to $377 million.

Other expenses rose by 22% over 1985 to $541 million. The most significant factors behind this increase were the new 1% federal capital tax directed at banks and the imposition of higher deposit insurance premiums. Increases in these two items amounted to $25 million and $17 million respectively. In addition, other business and capital taxes rose $14 million over 1985.

Higher costs of foreign operations arising from the lower-valued Canadian dollar added $23 million to expenses in 1986. This effect, however, is typically counterbalanced by higher foreign currency revenues when expressed in Canadian dollars.

CHART 13
Non-Interest Expenses
(% of Average Assets)

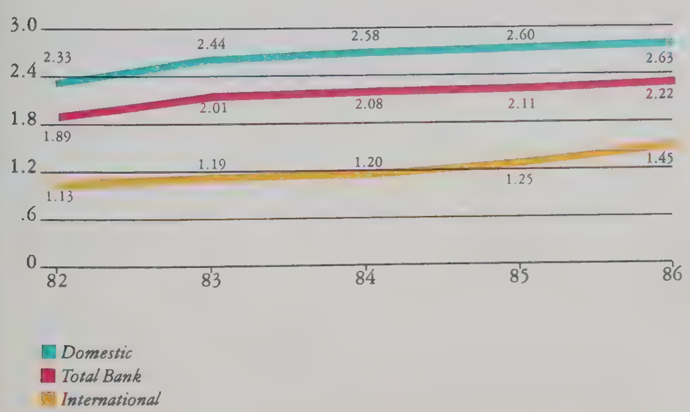


Table 9

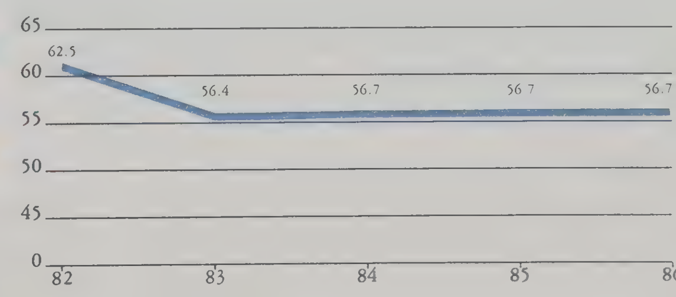
NON-INTEREST EXPENSES
($ Millions)

	1986	*1985*	*% Change*
Salaries, pensions and other staff benefits	**$1,254**	$1,180	6.3%
Premises and equipment			
Building rent	**106**	98	8.2
Less: rental income from subleases	**(45)**	(45)	—
	61	53	15.1
Depreciation	**116**	98	18.4
Computer rental and maintenance	**69**	63	9.5
Building repairs and maintenance	**42**	36	16.7
Property taxes	**34**	30	13.3
Furniture rental and maintenance	**28**	24	16.7
Other	**27**	22	22.7
	377	326	15.6
Other			
Business and other taxes	**90**	51	76.5
Telephone and telegraph	**63**	58	8.6
Stationery and printing	**62**	57	8.8
Travel and relocation	**52**	45	15.6
Postage and courier	**51**	45	13.3
Legal and professional fees	**43**	42	2.4
Deposit insurance	**28**	11	154.5
Other	**152**	133	14.3
	541	442	22.4
Total	**$2,172**	$1,948	11.5%

Excluding the increases in business and capital taxes, deposit insurance premiums, and the foreign currency translation effect, the year's growth in non-interest expenses would have been 7%.

To put the Bank's non-interest expenses into perspective, it is helpful to look at how much it costs the Bank to generate each dollar of revenue. This measure of productivity is calculated as the ratio of non-interest expenses to the sum of net interest income and other income. Chart 14 shows that this ratio has remained essentially unchanged over the past four years. This figure should improve in the years ahead as the Bank pursues productivity enhancement and expenditure control while retaining a strong commitment to superior customer service.

CHART 14
Non-Interest Expenses
(% of Net Interest and Other Income)



Income Taxes

The Royal Bank's reported provision for income taxes amounted to $175 million in 1986, declining $25 million from 1985.

Like other corporations in Canada, the Bank is subject to a combined provincial and federal statutory income tax rate of approximately 50%. An examination of the 1986 statement of income, however, reveals an effective tax rate of approximately 26%. This lower effective rate is caused by two important factors: the tax-exempt nature of certain securities, primarily "loan substitute" securities, and the lower rates of tax experienced by many foreign subsidiaries.

The Bank earns a substantial amount of tax-exempt income on its $1.9 billion portfolio of loan substitutes, comprised of small business bonds, income debentures, and term preferred shares. However, because the Bank does not pay taxes on this income, it is forced to accept a lower rate of interest or dividend than would apply to a loan of equal value, thus enabling the issuer to raise funds more cheaply. The effect of this reduction in income is reflected in net interest income in the Statement of Income. Although the reported income taxes may appear to be low, the Bank is effectively "paying taxes" by accepting a reduction in its reported net interest income in return for the tax-exempt status of the remaining income received.

For analytical purposes, a taxable equivalent adjustment, as explained earlier in the Net Interest Income section of this report, is made to compensate for tax-exempt earnings. Were the reported tax expense adjusted to reflect this differential, the provision for income taxes shown in the Statement of Income would increase by $174 million in 1986 and by $175 million in 1985, appearing as $349 million and $375 million respectively.

The Bank's lower effective income tax rate also results from the fact that many consolidated foreign subsidiaries are subject to lower rates of income taxes in their home countries than the approximate 50% tax rate applicable to the Royal Bank within Canada.

A reconciliation of the combined federal and provincial statutory income tax rates with the effective income tax rates for 1986 and 1985 is provided in Note 2 to the Financial Statements on page 65.

The taxable equivalent rate, however, does not in itself constitute a complete measure of the Bank's overall tax burden, since there are a number of other areas in which the Bank is taxed indirectly. First, each Canadian bank is required to maintain a certain portion of its deposits in the form of non-interest earning reserves with the Bank of Canada. In 1986, the Royal Bank maintained an average reserve deposit of approximately $1.4 billion. Using an average interest rate of 10%, the amount of interest foregone by the Bank, which may be looked upon as an indirect tax paid to the federal government, amounted to $140 million. Also, as mentioned previously in the Non-Interest Expenses section of this report, business and capital taxes rose significantly in 1986 to $90 million, due in large measure to the effect of the new 1% federal capital tax imposed on the banks in May 1985. Finally, in 1986 the Bank paid a variety of property taxes amounting to $34 million.

Portfolio Risk Management

The publication late in the year of the federal government's Estey Commission report on the collapse in 1985 of two small banks in western Canada focussed public attention on the issues of risk concentration and asset quality. Its findings reaffirmed that a bank's profitability and stability ultimately depend on the soundness of its credit policies.

The key principles involved in managing risk in a bank's loan portfolio are credit quality and diversification. The first consideration is to ascertain the soundness of each individual loan proposal. Subsequently, it is essential to vary the loans in the portfolio both by industry and by geographical location in order to ensure that overall earnings are not seriously impaired due to adverse conditions that may develop in any one industry or region.

With respect to risk concentration, it is the Royal Bank's policy to limit individual borrower loan authorizations to 15% of the Bank's shareholders' equity, except in the case of a select number of independent corporate borrowers, where this figure can be as high as 25%. As of October 31, 1986, there were only two borrowers with outstanding loan balances in excess of 15% of the Bank's shareholders' equity. Country and industry lending takes social, political and economic factors into consideration in addition to strategic objectives. Loan exposures are monitored closely and reviewed frequently in order to remain current with the most recent developments in both domestic and international affairs.

At the Royal Bank, credit quality is monitored by a sophisticated management information system, called the Risk Asset Monitoring System. Essentially, this system has the capability of monitoring the Bank's loan portfolio across several dimensions, including loan quality and industry and geographic exposure. With regard to loan quality, each credit risk is assigned a borrower risk rating, which is initially determined by the Bank's field officers and subsequently reviewed and confirmed at each successive stage of the credit process. The largest credits are reviewed by the Bank's Credit Policy Committee on a regular basis and ratings are confirmed or amended as appropriate. In addition to loan authorizations, the Risk Asset Monitoring System tracks authorizations, commitments, guarantees, letters of credit, and other off-balance sheet items.

The accompanying tables illustrate the diversification of the Royal Bank's Domestic and International assets. Table 10 provides a breakdown of the Bank's earning assets and portrays the geographic diversification of its loan portfolio. Domestic loans are classified by industry or type of loan as well as by province. The table demonstrates the Bank's active participation in each Canadian geographic and industry market sector.

The Bank also conducts extensive financing activities outside Canada. This is a direct result of the broad global commercial interests of its clients both in Canada and abroad. In addition to creating profit opportunities for the Bank and further broadening the base of its loan portfolio, the extension of credit to borrowers in foreign countries often facilitates and stimulates the sale of Canadian goods and services to these countries.

Table 10

Breakdown of Loans
As at September 30
($ Millions)

	1986	Per Cent	1985	Per Cent
Domestic				
Atlantic Provinces	$ 3,058	6.5%	$ 2,794	6.2%
Quebec	6,433	13.6	5,814	12.9
Ontario	16,590	35.1	15,211	33.8
Manitoba	2,347	5.0	2,252	5.0
Saskatchewan	2,702	5.7	3,030	6.7
Alberta	8,148	17.3	8,426	18.7
British Columbia	7,954	16.8	7,505	16.7
	47,232	100.0	45,032	100.0
Of which:				
Mortgages	12,585	26.6	10,495	23.3
Loans to individuals	10,120	21.4	9,245	20.5
Agricultural	2,207	4.7	2,317	5.1
Financial institutions	2,791	5.9	3,162	7.0
Merchandisers	3,287	7.0	2,886	6.4
Manufacturing	3,668	7.8	3,724	8.3
Construction	1,836	3.9	1,781	4.0
Mining and energy	3,907	8.3	3,762	8.4
Other	6,831	14.4	7,660	17.0
	47,232	100.0	45,032	100.0
International				
Canadian Risk	909	5.0	899	4.7
U.S.A.	4,729	25.8	4,802	24.9
Europe, Middle East and Africa	5,001	27.3	5,498	28.6
Latin America and Caribbean	6,166	33.6	6,156	32.0
Asia Pacific	2,150	11.7	2,231	11.6
General provision for losses on country lending	(628)	(3.4)	(357)	(1.8)
	18,327	100.0	19,229	100.0
Total Loans	65,559	73.0	64,261	73.6
Securities	9,931	11.1	8,819	10.1
Deposits With Other Banks	14,302	15.9	14,191	16.3
Total Earning Assets	$89,792	100.0%	$87,271	100.0%

By engaging in foreign lending, the Bank incurs potentially higher than normal risks due to the possiblity of such factors as unforseeable adverse political or economic developments. Consequently, the Bank monitors closely all international lending activity, limiting risk concentration on a country-by-country basis in addition to broad economic classifications of country groups.

Table 11 illustrates the distribution of the Bank's earning assets according to the development classification of the country of ultimate risk. While the "low income" and "lower middle income" countries represent 2.4% of earning assets, advances to borrowers in "industrialized" countries constitute 88% of the $89.8 billion total.

Table 12 provides an additional indication of the diversity of the Bank's international risk, showing earning assets for individual countries where the balances outstanding, including loans funded in local currencies, exceed one-half of one percent of total earning assets. The only foreign countries which account for more than 5% of the Bank's total earning assets are the United States and the United Kingdom.

The abrupt decline in the price of crude oil at the beginning of fiscal 1986 had severe consequences for highly-leveraged oil and gas companies worldwide. In addition, countries such as Mexico, whose export earnings are heavily dependent on oil revenue, were impacted severely by the sudden collapse of world oil markets. These events, coupled with the continuing problem of depressed prices for a number of other commodities, resulted in both loan restructurings and the adoption of new economic measures in Mexico as well as in other Third World nations.

The following discussion briefly summarizes the current state of the international debt situation, including the Bank's involvement with the major troubled country borrowers in Latin America, and a short analysis of current economic conditions in these countries.

Table 11

DISTRIBUTION OF EARNING ASSETS (1)
BY COUNTRY CLASSIFICATION
As at September 30
($ Millions)

	1986	*Per Cent*	*1985*	*Per Cent*
Industrialized countries	$79,323	88.3%	$76,370	87.5%
Centrally-planned industrialized countries	366	.4	531	.6
High income oil-exporting countries	227	.2	243	.3
Upper middle income countries	8,425	9.4	8,404	9.6
Lower middle income countries	1,582	1.8	1,716	2.0
Low income countries	497	.6	364	.4
General provision for losses on country lending	(628)	(.7)	(357)	(.4)
Total	$89,792	100.0%	$87,271	100.0%

(1) Earning assets are defined as all assets except Cash and deposits with the Bank of Canada, Acceptances, Land, buildings and equipment and Other assets. The distribution is based on International Bank for Reconstruction and Development classification of per capita income.

The International Debt Issue
The approach to dealing with the international debt issue has evolved considerably in the past year. Largely as a result of the initiative launched by U.S. Treasury Secretary Baker in October 1985, a strong consensus has emerged on the need for developing countries, with the support of official and private creditors, to encourage growth through structural economic reforms that would increase the role played by market forces in their economies.

Over the past several months, a number of developing countries – Argentina, Brazil and Mexico among them – have taken major steps towards structural economic adjustment. Official and private creditors have welcomed these steps as being in line with the Baker process.

Major industrial country governments have also endorsed the process of growth-oriented economic adjustment. These countries have specifically recognized their responsibility to foster a world economic environment conducive to developing country growth and made a commitment to closer policy coordination in order to enhance world growth. Over the course of 1986, the continued reduction in international interest rates has significantly reduced debtor countries' interest payments.

Argentina
At September 30, 1986, the Royal Bank's exposure in Argentina totalled $479 million, or 0.5% of earning assets. Of this amount, $38 million was classified as non-accrual.

The setback suffered in export earnings as a result of low grain prices and flood damage in 1986 has not diverted the broad thrust of policy from structural economic reform. The emerging industrial strategy emphasizes the role of the private sector and aims to strengthen export-oriented activities. The strong anti-inflation measures introduced in June 1985 with the Austral plan are being complemented by reforms in the trade, agriculture and financial sectors now being developed with considerable financial support from the World Bank.

The first half of 1986 saw a strong resurgence of growth which led, however, to an acceleration of inflation. In early September, the government took steps to tighten monetary policy and reduce price and wage increases paving the way to a new round of negotiations with the IMF on a financing package for 1987-88. Mini-devaluations, particularly since August 1986, have ensured continued price competitiveness in international markets.

Brazil
At September 30, 1986, the Bank's exposure in Brazil was $1.6 billion, or 1.8% of the Bank's earning assets, $1 million of which was classified as non-accrual.

A bold anti-inflation plan – The Cruzado plan – was introduced in February 1986. The monthly rate of inflation fell sharply from 16% in January to less than 2%. This policy was reinforced in July with the introduction of measures aimed at curbing booming domestic demand which threatened to overheat the economy. Special levies on car and fuel sales and international travel were introduced to finance the newly created "National Development Fund" which will be used to undertake major investments in key sectors over the next three years. An austere budget proposed for 1987 should set the stage for structural reform through increased fiscal discipline.

Brazil's reform efforts have coincided with a very strong growth performance. Real GDP in 1986 is estimated to have increased about 7% after the 8.3% rate recorded in 1985.

Table 12

DISTRIBUTION OF EARNING ASSETS (1) BY LOCATION OF ULTIMATE RISK

As at September 30

($ Millions)

	Total Earning Assets				Loans			
	1986	*Per Cent*	*1985*	*Per Cent*	*1986*	*Per Cent*	*1985*	*Per Cent*
Canada	$55,571	61.9%	$53,950	61.8%	**$48,141**	73.4%	$45,931	71.5%
United States	9,224	10.3	9,637	11.0	4,729	7.2	4,802	7.5
Europe, Middle East and Africa								
United Kingdom	4,936	5.5	4,309	4.9	2,004	3.1	1,882	2.9
France	1,331	1.5	943	1.1	150	.2	173	.3
West Germany	1,171	1.3	895	1.0	483	.7	337	.5
Switzerland	931	1.0	531	.6	157	.2	102	.2
Belgium	816	.9	851	1.0	317	.5	440	.7
Italy	261	.3	433	.5	106	.2	295	.5
Other	2,944	3.3	3,375	3.9	1,784	2.7	2,269	3.5
	12,390	13.8	11,337	13.0	5,001	7.6	5,498	8.6
Latin America and Caribbean								
Brazil	1,629	1.8	1,442	1.7	1,362	2.1	1,418	2.2
Mexico	1,557	1.7	1,603	1.8	1,525	2.3	1,560	2.4
Venezuela	720	.8	762	.9	720	1.1	752	1.2
Bahamas	664	.7	611	.7	511	.8	453	.7
Argentina	479	.5	455	.5	464	.7	429	.7
Other	1,753	2.0	1,933	2.2	1,584	2.4	1,544	2.4
	6,802	7.5	6,806	7.8	6,166	9.4	6,156	9.6
Asia Pacific								
Japan	3,744	4.2	3,406	3.9	522	.8	490	.8
Hong Kong	507	.6	409	.5	273	.4	185	.3
South Korea	449	.5	445	.5	405	.6	396	.6
Australia	398	.4	517	.6	182	.3	320	.5
Other	1,335	1.5	1,121	1.3	768	1.2	840	1.2
	6,433	7.2	5,898	6.8	2,150	3.3	2,231	3.4
General provision for losses on country lending	(628)	(.7)	(357)	(.4)	(628)	(.9)	(357)	(.6)
Total	$89,792	100.0%	$87,271	100.0%	$65,559	100.0%	$64,261	100.0%

(1) Earning assets are defined as all assets (including assets funded in local currencies) except Cash and deposits with Bank of Canada, Acceptances, Land, buildings and equipment and Other assets. Individual countries are indicated where assets exceed ½ of 1% of earning assets.

Mexico

At September 30, 1986, the Royal Bank's exposure in Mexico totalled $1.6 billion, or 1.7% of earning assets. Of this amount, $108 million was classified as non-accrual.

The collapse in oil prices in 1986 and a loss in market share early in the year translated into a US$8 billion loss in export revenues for Mexico as well as a sharp upturn in government financing requirements. Prospects of continued severe austerity (the Mexican economy is estimated to have contracted by 3% in 1986) prompted the government to negotiate a comprehensive economic reform program aimed at resuming growth with the assistance of the IMF, other multilateral institutions and commercial banks. The basic thrust of the program is the liberalization of the economy, leading to strong international competitiveness and lesser dependence on oil revenues. The progressive reduction of the large role of government in the economy should result in increased private sector investment while progress in closing the gap between the free and controlled exchange rate should promote exports and eliminate previous trade distortions. World Bank financing is specifically destined to support trade liberalization measures in harmony with Mexico's decision in July 1986 to join the protocol of the General Agreement on Tariffs and Trade.

Venezuela

At September 30, 1986, the Bank's exposure in Venezuela totalled $720 million, or 0.8% of total earning assets, $54 million of which was classified as non-accrual.

The implementation of Venezuela's public investment plan to promote economic recovery was delayed in 1986 by the sharp loss in anticipated oil revenues. While a recession was avoided, real growth was minimal. Economic activity should accelerate in 1987, in line with the government budget proposal to go ahead with planned public investment activities.

The relatively high international reserve position of Venezuela has cushioned the balance of payments implications of the fall in oil prices but the authorities have asked the creditor banks to reopen the multi-year rescheduling agreement signed in 1986 in order to arrive at a new, stretched-out debt repayment schedule.

Table 13

INTEREST RATE SENSITIVITY POSITION
As at October 31, 1986
($ Billions)

	Less than 1 Month	*1 to 3 Months*	*3 to 6 Months*	*6 to 9 Months*	*9 Months to 1 Year*	*Over 1 Year*
Canadian Dollar Operations						
Period total	($4.5)	$2.5	($0.2)	$0.6	$0.8	$0.8
Cumulative position	($4.5)	($2.0)	($2.2)	($1.6)	($0.8)	$0.0
Foreign Currency Operations						
Period total	($2.4)	($0.8)	$0.1	($0.1)	$0.2	$3.0
Cumulative position	($2.4)	($3.2)	($3.1)	($3.2)	($3.0)	$0.0
Total Bank						
Period total	($6.9)	$1.7	($0.1)	$0.5	$1.0	$3.8
Cumulative position	($6.9)	($5.2)	($5.3)	($4.8)	($3.8)	$0.0

INTEREST RATE SENSITIVITY AND LIQUIDITY MANAGEMENT

Interest Rate Sensitivity

Interest rate sensitivity is defined as the rapidity with which average yields on earning assets and average rates paid on interest-bearing liabilities respond to changes in prevailing rates of interest. Interest rate risk is introduced when assets and the liabilities used to fund them do not respond to changes in interest rates concurrently. A key determinant of interest rate sensitivity is the repricing date – the timing of the next opportunity to adjust the interest rate to new market levels. Mismatches in repricing dates of assets and liabilities are frequently referred to as "interest rate gaps". A "negative" interest rate gap exists when more liabilities are subject to repricing earlier than assets; a "positive" interest rate gap indicates the reverse.

As a general rule, when interest rates fall, and a negative gap exists, the net interest margin will be enhanced for a period of time – for example, when a one-year mortgage loan is funded by a one-month term deposit. Given no further changes in rates, this revenue-enhancing effect will continue until the mortgage repricing date is reached. Should the prevailing rates of interest increase, and a negative gap position exists, the opposite occurs: the net interest margin is compressed. If the situation is one in which assets, such as prime-rate loans, are more interest rate sensitive than liabilities (a positive gap position), reductions in interest rates compress margins, while rising interest rates increase margins.

In a situation where cumulative gap positions exist only at shorter terms, unfavourable interest rate movements will have less of an adverse impact on earnings over time than if the cumulative positions existed for longer terms.

In all cases, the extent to which the net interest margin is affected will depend upon the degree and rapidity of change in interest rate levels, the size of the cumulative gap positions, and the maturity terms at which the gap positions exist.

In the financial intermediation process, varying term preferences of customers in the deposit and lending functions initially result in the assumption of gap positions. Management of these gap positions is a highly important determinant of bank profitability. To the extent that a position is matched, the risk caused by a future interest rate change is eliminated. However, the assumption of this risk-free position also results in reduced overall profit potential. Opportunities for enhanced returns arising from mismatched positions and favourable interest rate movements are constantly weighed against the costs that could arise from unfavourable interest rate changes and the need to respect liquidity policy guidelines.

During 1986, the correct anticipation of downward trending rates with low volatility provided an opportunity for the taking of larger gap positions at a profit, which added to the Bank's earnings.

In Domestic operations, growth in mortgage balances combined with a change in customer preferences for longer terms gave rise to changed gap profiles. These were successfully managed within prudential corporate limits and at a profit through the use of the medium-term capital markets.

In International operations, the Bank closely manages the projected net cash flows to control the adequacy of liquidity in all major market areas. Liquidity factors take precedence over interest rate exposure factors, and sometimes forced gap positions may result. However, interest rate gaps caused by liquidity considerations in the Bank's foreign currency business typically are not significant.

The Bank's interest rate sensitivity position as at October 31, 1986 is highlighted in Table 13. We have identified the portfolio mismatch at the one-month, three-month, six-month, nine-month and one-year time horizons. The figures indicate positions at which earnings may potentially be affected by interest rate changes if no action is taken. The cumulative gap positions represent the sum of all gap figures at or before the repricing date shown.

The gains and losses on the Bank's fixed-rate debt trading portfolios are reflected regularly by the use of a mark-to-market procedure. A "proxy" gap position, reflecting a weighting of the full term of these portfolios, is included in the one year and under gap positions shown in this table. As is apparent, interest rate gaps of significance are confined primarily to the shorter-term maturities. At the one-year point, the Bank has a cumulative negative gap position of approximately 4% of total assets, virtually unchanged from one year ago.

These figures should be viewed with caution since they indicate a position at only one point in time, and significant changes in positions can and are made quickly depending upon client demands and the Bank's view of future interest rate movements.

The Bank's success in the asset/liability management process was due in no small part to its access and participation in worldwide financial markets via its strategically enhanced investment banking capabilities.

At the Royal Bank, the management of interest rate sensitivity and liquidity positions worldwide, including those in currencies other then Canadian dollars, is the specific responsibility of the Treasury function within the Corporate / Investment Banking and Treasury Group. Certain activities are conducted through units based in major financial centres around the world, but are coordinated and controlled by Head Office.

Liquidity Management

The main focus of liquidity management is to ensure the continuing ability to meet customer deposit withdrawals and maturities and satisfy worldwide borrowings, repayments, and credit commitments in a timely manner.

Liquidity is maintained through close coordination of asset and liability management on a bank-wide basis. A cornerstone of the Bank's liquidity management policy is the maintenance of a highly diversified deposit base. Note 8 to the Financial Statements on page 67 provides a detailed breakdown of the Bank's total deposits and, in particular, indicates the extent of the Bank's "core" deposits in the "payable after notice" classification and other deposits by individuals. The growth of these "core" deposits is highlighted in Chart 10 on page 36. Other major elements of the Bank's overall liquidity management capabilities are: close management of loan and deposit maturity structures; policy limits which govern the maximum net outflow of funds which should be scheduled for a given time frame; and access to liquid assets and committed credit lines.

In Canada, the Bank currently maintains $1.4 billion of primary reserves, including cash and deposits with the Bank of Canada, and an additional $1.4 billion of secondary reserves invested in short-term Government of Canada securities as required by law. In addition to these statutory liquidity reserves, the Bank, under established internal policies, maintains supplementary reserves in the form of very liquid assets, which amounted to $1.3 billion at October 31, 1986. The Bank also has access to the Bank of Canada, which functions as lender of last resort to the Canadian banking system.

Internationally, the cornerstones of liquidity management are: diversification of world-wide funding sources; close control of the maturity profiles of loan and deposit portfolios; policy limits governing net cash outflow; and supplementary reserves in very liquid foreign assets. As a major participant in the Eurodollar market, the Bank has access to deposits from other large international banks and, in turn, places redeposits with other large banks for short terms.

In 1986, the Bank continued to follow conservative liquidity management practices. Domestically, this was reflected in the previously noted high levels of supplementary liquidity reserves while internationally, year-end interbank redeposits of $12.6 billion represented 29% of foreign currency assets. Throughout the year, increased emphasis was placed on the lengthening of deposit terms through the use of capital markets. Where appropriate, this activity was coupled with the use of "synthetic" interest rate management products to manage gap position objectives.

Table 14

Change in Capital Funds

For the year ended October 31
($ millions)

	1986	*1985*	*1984*	*1983*	*1982*
Net income	$489	$488	$450	$480	$358
Excess of loss experience on loans over provision for loan losses	(158)	(64)	(207)	(320)	(336)
Income tax credit on transfer to appropriations for contingencies	86	82	91	86	94
Other	(21)	(4)	(12)	—	21
Capital from operations	396	502	322	246	137
Less dividends	(281)	(268)	(247)	(218)	(201)
Internally generated capital	115	234	75	28	(64)
External sources of capital					
Common stock	231	192	142	96	43
Preferred stock	148	—	226	292	203
Debentures	318	414	216	(2)	342
Total external sources of capital	697	606	584	386	588
Total increase in capital	$812	$840	$659	$414	$524

Capital Funds Management

Capital funds include common and preferred shareholders' equity, appropriations for contingencies, and subordinated debentures. In its broadest sense, the role of capital is to maintain the full confidence of depositors, creditors and shareholders in the integrity and stability of the Bank. An adequate capital base is viewed as an important component of the Bank's capacity to absorb any unforeseen and unusually severe setbacks which might otherwise impair its ability to continue operating as a going concern. Capital also provides the funds needed to acquire fixed assets, such as branch facilities and computer equipment which are necessary to conduct the business of banking. Finally, growth in capital funds is a prerequisite to the continuing expansion of credit and other banking services.

A primary objective of management is to provide the common shareholders with a competitive return on investment. Supplementing the common shareholders' investment with long-term debt and preferred shares is an effective means of helping to achieve this goal. Capital funds management involves balancing the long-term safety and growth needs of the Bank with the return-on-investment expectations of shareholders.

Capital funds totalled $6.7 billion at the end of 1986, an increase of $812 million or 14% over last year. During fiscal 1986 the Bank raised $231 million in common equity, $129 million from the Bank's Shareholder Dividend and Share Purchase Plan, and $102 million from the issue of three million common shares just prior to year end. In addition, in April 1986 the Bank issued $150 million in price-adjusted floating rate preferred shares, and in June 1986 it issued U.S. $300 million (approximately CAN. $417 million) in floating-rate 99-year subordinated debentures. The interest rate payable on these "permanent" debentures is adjustable downwards in the event of a reduction in the current level of dividends paid on common shares. Both the "permanent" debentures and the price-adjusted preferred shares are eligible to qualify as base capital. Partially offsetting the above increases was a reduction of $100 million due to maturing debentures.

A five-year history of changes in capital funds appears in Table 14. As the table shows, most of the Bank's growth in capital over that period stems from external sources. The amount of internally-generated capital was down substantially in 1986 due entirely to the excess of loan loss experience over the provision for loan losses. In 1986 this excess amounted to $158 million compared to $64 million

Chart 15
Capital Funds
($ Millions)

Table 15

CAPITAL RATIOS

As at October 31

($ millions)

	1986	*1985*	*1984*	*1983*	*1982*
Total assets per balance sheet	**$ 99,607**	$ 96,017	$88,003	$84,682	$88,456
Letters of credit and guarantees	**5,551**	4,808	4,400	3,595	3,421
Less investment in associated corporations (20%–50% owned)	**(154)**	(154)	(110)	(95)	(83)
Gross assets for capital ratios	**$105,004**	$100,671	$92,293	$88,182	$91,794
Base capital					
Common shareholders' equity	**$3,536**	$3,190	$2,763	$2,549	$2,428
Permanent preferred shares (1)	**689**	537	531	300	—
Permanent debentures (1)	**186**	—	—	—	—
Appropriations for contingencies	**101**	101	103	100	101
Less investment in associated corporations (20%–50% owned)	**(154)**	(154)	(110)	(95)	(83)
Minority interests	**9**	9	8	5	2
Total base capital	**4,367**	3,683	3,295	2,859	2,448
Supplementary capital					
Non-permanent preferred shares (2)	**210**	256	345	350	354
Non-permanent debentures (2)	**1,308**	1,411	1,011	856	950
Permanent debentures	**231**	—	—	—	—
Total supplementary capital	**1,749**	1,667	1,356	1,206	1,304
Adjusted total capital (base & supplementary)	**$6,116**	$5,350	$4,651	$4,065	$3,752
Base capital to gross assets	**4.2%**	3.7%	3.6%	3.2%	2.7%
Base capital equivalent to gross assets (3)	**4.7%**	4.2%	4.0%	3.7%	3.2%
Adjusted total capital to gross assets	**5.8%**	5.3%	5.0%	4.6%	4.1%

(1) The aggregate amount of permanent preferred shares and debentures which may be included in base capital is limited to 20%.

(2) Securities which are within five years of maturity are subject to straight line amortization to zero during their remaining term and, accordingly, are included above at their amortized value.

(3) Base capital equivalent is equal to the sum of base capital and one-third of supplementary capital.

in 1985. As a result, internally generated capital amounted to $115 million in 1986 versus $234 million in the previous year.

Table 15 presents the Bank's capital ratios, using definitions developed by the Office of the Inspector General of Banks. Base capital includes those elements of capital funds which are permanent, subordinate to other creditors and are free of mandatory fixed charges against earnings. The individual components of base capital are shown in Table 15 and include common shareholders' equity and appropriations for contingencies, as well as permanent preferred shares and debentures, with the latter two instruments limited to a 20% proportion of total base capital. Supplementary capital comprises those instruments such as debentures and redeemable preferred shares which, although subordinate to the right of depositors, do not have all of the required properties of base capital. Adjusted total capital is the sum of base capital and supplementary capital. Base capital equivalent is defined as base capital plus one-third of supplementary capital.

In 1986 the Bank's base capital to gross assets ratio rose to 4.2% from 3.7% in 1985. Similarly, both the base capital equivalent ratio and the adjusted total capital ratio increased to 4.7% and 5.8% respectively. It is evident from these measures that the Bank's capital position grew increasingly stronger over the course of the year, adding further to the significant improvement achieved in this area during the past five years.

While the ratios reported in Table 15 are useful indicators of the progress made in raising overall capital levels, ratios alone do not constitute a thorough assessment of the adequacy of a bank's capital base. More important and perhaps less quantifiable measures of a bank's stability are its management capability, the stability of its funding sources, the diversity of its loan portfolio and earnings streams, and its market position. We believe that all of these areas represent significant strengths of the Royal Bank.

The Bank holds a broad base of personal deposits, which, as disclosed elsewhere in this report, amounted to $41.0 billion worldwide at October 31, 1986. This core consumer deposit base permits minimal dependence on more volatile funding sources and, as such, is an important factor in the Bank's stability.

Another significant issue in the discussion of capital adequacy is the effect of the Bank's relative liquidity position. While the high levels of liquidity that are maintained by the Bank have the effect of reducing reported capital ratios, it should be appreciated that such balances greatly increase the Bank's flexibility, and thus, its stability during periods of unsettled financial markets.

It is also noteworthy that the Royal Bank has a substantial investment in fixed assets, including land and buildings in Canada and abroad which are carried on the balance sheet at a net book value of $688 million. While there is no intention of disposing of these assets, management estimates that these properties have a market value which is more than $500 million greater than the reported book value.

In addition, it should be noted that at January 1, 1986, the Bank's pension fund had a funding excess of $226 million. This surplus, which represents the difference between the adjusted market value of pension fund assets and the present value of accrued pension benefits, is not factored into any regulatory measurement of capital adequacy.

All things considered, the Bank has a very sound capital position, which compares favourably with those of its domestic and international competitors. In the periods ahead, the Bank intends to ensure the continued improvement and development of this solid capital base.

Readers are cautioned that direct comparisons of Canadian capital ratios with those reported by banks in other countries are generally not meaningful. Important definitional differences make such comparisons inappropriate. For example, the primary capital base for U.S. banks, as defined by regulators in that country, includes the allowance for loan losses. In Canada, such amounts are deducted from loan balances outstanding and are excluded from the calculation of base capital. In addition, in contrast to the Canadian practice, U.S. banks do not include off-balance sheet commitments such as letters of credit and guarantees in the determination of their capital ratios, nor do they reduce primary capital for investments in associated corporations. Generally, Canadian capital ratios are based upon definitions that include broader groups of assets and more restrictive definitions of capital than those used by many foreign regulators.

Off-Balance Sheet Activities

The Royal Bank offers a variety of off-balance sheet products to its customers to meet their needs for liquidity and for foreign exchange and interest rate protection. Many of these latter products have been developed in recent years within increasingly sophisticated financial markets. The Bank also uses some of these same products in order to reduce its own exposure to movements in interest rates and foreign exchange. All off-balance sheet products are subject to the Bank's normal credit standards, financial controls, and risk limiting and monitoring procedures.

In the past year, bank regulators in Canada and other countries have been directing attention to the extent of banks' involvement in off-balance sheet activities, the risk associated with such activities, and in particular the degree of risk which should be factored into capital adequacy requirements. It is the Royal Bank's view that the degree of risk associated with its off-balance sheet activities is relatively small and can be accommodated by modest amounts of capital.

In Table 16, a detailed breakdown is provided of the Bank's various off-balance sheet activities, expressed in terms of the principal or nominal value of the related commitment or contract. For ease of discussion, the various items have been grouped under two main headings – liquidity products and foreign exchange and interest rate contracts.

Liquidity Products

Liquidity products are those whose primary purpose is to ensure that funds are available to a customer as required. Such products include guarantees and letters of credit as well as commitments to extend credit.

Guarantees and Standby Letters of Credit primarily represent irrevocable assurances that the Royal Bank will make payment in the event that its customer cannot meet its financial obligations to third parties. Certain other guarantees represent non-financial undertakings such as bid and performance bonds.

Documentary and Commercial Letters of Credit are established for the purpose of facilitating international trade and represent written undertakings by the Bank on behalf of its customer (typically an importer), authorizing a third party, an exporter, to draw drafts on the Bank up to a stipulated amount under specific terms and conditions.

Table 16

Off-Balance Sheet Activities

As at September 30, 1986
($ Millions)

Liquidity Products –	
Guarantees and Standby Letters of Credit	$ 3,055
Documentary and Commercial Letters of Credit	2,276
Commitments to Extend Credit (1)	
General	27,653
Firm – with a term less than or equal to 1 year	12,445
– with a term greater than 1 year	2,301
Note Issuance Facilities/Revolving Underwriting Facilities	1,387
Foreign Exchange and Interest Rate Contracts –	
Foreign Exchange Forward Contracts (2)	120,119
Foreign Currency and Interest Rate Futures	5,232
Future Rate Agreements	2,514
Foreign Currency and Interest Rate Options	389
Foreign Currency and Interest Rate Swaps	16,965

(1) Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, bankers' acceptances, guarantees or letters of credit.

(2) Foreign exchange forward contracts represent commitments to purchase foreign currency and Canadian dollars, including undelivered spot transactions.

With respect to risk, guarantees and letters of credit are no different than loans and other assets reflected on the balance sheet. As a result, as shown in Table 16, these commitments are already factored into existing capital adequacy rules.

Commitments to Extend Credit represent credit facilities available to clients, either in the form of loans, bankers' acceptances and other on-balance sheet financings or through off-balance sheet products such as guarantees and letters of credit. While quantification of the risk associated with commitments to extend credit is not obvious, the amount of risk is considerably less than the total unused commitments.

To illustrate, most commitments to extend credit are contingent upon customers maintaining specific credit standards such as a minimum amount of tangible net worth and working capital, or minimum financial ratios. Inasmuch as this is the case, the credit risk associated with such commitments, designated as "general" in Table 16, is virtually eliminated. While there is some credit risk associated with the remainder of commitments described as "firm", the risk is viewed as modest since it results firstly from the possibility of unused portions of loan authorizations being drawn by the customer and, secondly, from these drawings subsequently not being repaid as due. For risk management purposes, the Bank further subdivides "firm" credit commitments into those with a term of less than or equal to one year, and those with a term of greater than one year. The Bank's experience has been that longer-term commitments have a greater degree of risk than shorter-term commitments.

Note Issuance Facilities (NIF's) and Revolving Underwriting Facilities (RUF's) are arrangements whereby a customer issues short-term notes supported by an undertaking by the Bank that if the customer is unable to issue the notes at a predetermined price, that the Bank will buy them at that price. The Bank considers the risk associated with NIF's and RUF's to be comparable to that of longer-term "firm" commitments to extend credit.

Foreign Exchange and Interest Rate Contracts
Foreign exchange and interest rate contracts enable customers to transfer, modify or reduce their foreign exchange and interest rate risks. Such contracts include foreign exchange forward contracts as well as foreign currency and interest rate futures, options and swaps.

Foreign Exchange Forward Contracts represent commitments to purchase or sell a fixed amount of foreign currency at a set rate on a future specified date. The Bank enters into foreign exchange forward contracts both to service the needs of customers and to earn income as a trader in foreign exchange. In addition, the Bank uses such contracts to hedge the foreign exchange risk associated with its investments in foreign branches, subsidiaries and associated corporations. With the exception of hedging contracts, commitments entered into by the Bank to buy a fixed amount of one currency are generally offset by forward contracts to sell the same amount of that currency. The Bank maintains strict control limits on net open positions, that is, the difference between forward purchase and forward sale contracts, by currency and by term.

Foreign Currency and Interest Rate Futures are contractual obligations to buy or sell a foreign currency or a financial instrument, on a future date, at a specified price established on a commodity exchange. In addition to servicing customers' needs, the Bank utilizes interest rate futures both in trading activities, and in the management of interest rate risk associated either with specific assets and liabilities, or with balance sheet positions.

Future Rate Agreements are contracts which call for cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, on a notional principal amount, for a predetermined period. Future rate agreements, which are effectively tailor-made interest rate futures, are used by the Bank to service customers' needs and to manage interest rate risk.

Foreign Currency and Interest Rate Options are contractual agreements in which the writer of the option grants the purchaser of the option the future right, but not the obligation, to buy, or to sell, at or by a set date, a set amount of foreign currency or a financial instrument at a set price. The Bank enters into foreign currency and interest rate options as a writer in order to earn fee income, and as a purchaser in order to manage foreign currency exposure and interest rate risk.

Foreign Currency and Interest Rate Swaps are transactions in which two parties exchange currencies and/or the related interest flows i.e., fixed-rate for floating-rate, or vice versa, on a specified amount of notional principal for a specified period. The Bank enters into swaps as an intermediary between swapping counterparties in order to earn fee income, and as a principal in order to manage foreign currency and interest rate exposures.

Generally, the Bank manages the exposures related to foreign exchange and interest rate contracts either as part of overall borrowing limits granted to customers or as part of its trading activities. In either case, the related exposure can be analyzed in terms of market risk and credit risk, which is not really different than the way in which the exposures related to on-balance sheet items are examined. *It is important to recognize, however, that the amounts potentially at risk are just a small fraction of the principal amounts which are normally used to express the volume of foreign exchange and interest rate contracts outstanding.*

Market risk is essentially the exposure created by fluctuations in foreign exchange and interest rates. Market risk is not only a function of the volume of the transaction and the volatility of the underlying foreign exchange or interest rate but is also affected by the extent to which positions have offsetting exposures. Such offsetting exposures can take a variety of forms. Within products, for example, the foreign exchange exposure associated with a forward contract to purchase a certain amount of a foreign currency may be offset with a forward contract of identical term, to sell the same amount of the same currency. Alternatively, the exposure of an on-balance sheet asset or liability to exchange rate or interest rate changes may be offset by an off-balance sheet product such as a foreign exchange forward contract, a foreign currency or interest rate option, or swap, or some combination thereof. In all cases, the exposure of the Bank to market risk is controlled by strict trading limits and monitoring procedures.

Credit risk is the exposure to loss in the event of non-performance by the other party to a transaction, and is a function of the ability of the counterparty to honour its obligations to the Bank. For all types of foreign exchange and interest rate contracts, only exposures created by movements unfavourable to a customer's foreign exchange or interest rate position create a potential for credit risk. *Hence only half of the contract amounts outstanding will be a source of any credit risk at a particular point in time, and then only for an amount equal to changes in foreign exchange or interest rates.* The Royal Bank controls all credit risks through credit approvals, limits and monitoring procedures.

Finally, with respect to both market risk and credit risk, the exposure to loss bears a direct relationship to the term of the foreign exchange or interest rate contract. The Bank considers shorter-term contracts of, for instance, a duration of less than one year, to be of very low risk. On the other hand, contracts of greater than one year are considered by the Bank as potentially involving some risk, but of an amount which is relatively nominal for most instruments.

To summarize, as indicated by the figures in Table 16, the Royal Bank has extensive off-balance sheet activities in the form of liquidity products and foreign exchange and interest rate contracts. However, in most cases the amounts reflected are gross volume indicators only and do not represent the much smaller amount of potential risk exposure to which the Bank is subject. While the Inspector General of Banks in Canada, and other bank regulators worldwide have yet to adjust capital adequacy requirements for the risk associated with off-balance sheet activities, the Royal Bank believes that this risk is relatively small and can be accommodated by minimal amounts of capital.

Consolidated Statement of Income

For the Year Ended October 31 *($ Millions)*	*1986*	*1985*	*1984*	*1983*	*1982*	*1981*	*1980*	*1979*	*1978*	*1977*
Interest Income										
Loans	$6,922	$6,985	$6,968	$7,009	$9,361	$8,193	$5,006	$3,649	$2,533	$2,071
Lease financing	66	64	65	71	76	41	34	22	21	9
Securities	856	771	718	664	788	777	614	501	320	245
Deposits with banks	1,094	1,371	1,267	1,138	1,860	1,739	1,114	641	365	262
	8,938	9,191	9,018	8,882	12,085	10,750	6,768	4,813	3,239	2,587
Interest Expense										
Deposits	5,976	6,564	6,605	6,513	10,151	8,952	5,351	3,601	2,095	1,626
Bank debentures	172	147	120	127	129	71	49	45	34	28
Other	38	39	39	39	40	15	10	5	4	5
	6,186	6,750	6,764	6,679	10,320	9,038	5,410	3,651	2,133	1,659
Net Interest Income	2,752	2,441	2,254	2,203	1,765	1,712	1,358	1,162	1,106	928
Provision for loan losses	817	621	535	452	344	186	124	106	97	84
Net Interest Income After Provision for Loan Losses	1,935	1,820	1,719	1,751	1,421	1,526	1,234	1,056	1,009	844
Other income	904	818	709	667	583	500	378	321	271	245
Net Interest and Other Income	2,839	2,638	2,428	2,418	2,004	2,026	1,612	1,377	1,280	1,089
Non-Interest Expenses										
Salaries	1,147	1,076	1,014	977	945	784	664	575	494	444
Pension and other staff benefits	107	104	92	98	91	79	74	65	54	49
Premises and equipment, including depreciation	377	326	294	273	256	203	177	158	151	133
Other	541	442	404	398	382	318	275	213	181	159
	2,172	1,948	1,804	1,746	1,674	1,384	1,190	1,011	880	785
Net Income Before Income Taxes	667	690	624	672	330	642	422	366	400	304
Income taxes	175	200	173	191	(28)	160	61	60	136	114
Net Income Before Minority Interests	492	490	451	481	358	482	361	306	264	190
Minority interests in subsidiaries	3	2	1	1	0	4	13	16	3	2
Net Income	$ 489	$ 488	$ 450	$ 480	$ 358	$ 478	$ 348	$ 290	$ 261	$ 188
Income Per Share										
Basic	$4.05	$4.28	$4.25	$5.03	$3.87	$5.75	$4.74	$3.96	$3.57	$2.57
Fully diluted	$3.74	$3.91	$3.87	$4.58	$3.68	$5.71	$4.74	$3.96	$3.57	$2.57

Consolidated Statement of Assets and Liabilities

As at October 31

($ Millions)	*1986*	*1985*	*1984*	*1983*	*1982*	*1981*	*1980*	*1979*	*1978*	*1977*
Assets										
Cash resources	**$14,908**	$14,992	$15,648	$13,002	$15,018	$15,852	$11,142	$ 9,752	$ 7,463	$ 6,565
Securities	**10,244**	10,490	7,484	7,357	6,795	7,346	6,567	6,104	4,674	3,479
Loans	**65,934**	63,831	59,014	58,067	60,284	57,131	40,805	32,714	26,978	23,066
Customers' liability under acceptances	**5,438**	4,137	3,333	3,928	3,472	2,415	1,451	934	499	365
Land, buildings and equipment	**1,168**	1,028	947	915	861	810	733	621	544	478
Other assets	**1,915**	1,539	1,577	1,413	2,026	1,805	784	551	445	322
Total Assets	$99,607	$96,017	$88,003	$84,682	$88,456	$85,359	$61,482	[illegible]	[illegible]	[illegible]
Liabilities										
Deposits										
Payable on demand	**$ 7,281**	$ 7,638	$ 6,909	$ 7,985	$ 6,958	$ 7,048	$ 7,174	$ 6,044	$ 6,241	$ 5,183
Payable after notice	**24,980**	22,472	19,022	18,103	16,116	13,754	11,694	9,523	8,291	7,580
Payable on a fixed date	**51,992**	53,433	51,658	48,301	55,332	56,063	36,965	31,008	23,032	19,111
	84,253	83,543	77,589	74,389	78,406	76,865	55,833	46,575	37,564	31,874
Other liabilities										
Acceptances	**5,438**	4,137	3,332	3,928	3,472	2,415	1,451	934	499	365
Other	**3,177**	2,411	1,997	1,941	2,572	2,593	1,272	730	625	434
Minority interests in subsidiaries	**9**	9	8	5	2	6	177	165	14	9
	8,624	6,557	5,337	5,874	6,046	5,014	2,900	1,829	1,138	808
Subordinated debt										
Bank debentures	**2,068**	1,749	1,336	1,120	1,121	779	594	519	414	354
Capital and reserves										
Appropriations for contingencies	**101**	101	102	100	101	258	213	212	130	64
Shareholders' equity										
Capital stock – preferred	**1,025**	877	876	650	354	150	—	—	—	—
– common	**1,193**	962	771	629	85	83	80	73	73	73
Contributed surplus	—	—	—	—	452	408	348	193	193	193
Retained earnings	**2,343**	2,228	1,992	1,920	1,891	1,802	1,514	1,275	1,091	909
	4,662	4,168	3,741	3,299	2,883	2,701	2,155	1,753	1,487	1,239
Total Liabilities, Capital and Reserves	**$99,607**	$96,017	$88,003	$84,682	$88,456	$85,359	$61,482	$50,676	$40,603	$34,275

Net Interest Income on Average Assets and Liabilities

(For the year ended October 31)
($ Millions)

	1986			1985			1984		
	Average Balances	*Interest*	*Average Rate*	*Average Balances*	*Interest*	*Average Rate*	*Average Balances*	*Interest*	*Average Rate*
Assets									
Earning Assets									
Deposits with other banks	$13,441	$1,094	8.14%	$14,607	$1,371	9.39%	$13,182	$1,267	9.61%
Securities									
Loan substitutes	2,371	259	10.92%	2,644	294	11.12%	2,736	363	13.27%
Other securities	7,538	771	10.23%	5,615	652	11.61%	4,539	576	12.69%
	9,909	1,030	10.39%	8,259	946	11.45%	7,275	939	12.91%
Loans									
Domestic									
Mortgages and consumer instalment loans	16,957	2,020	11.91%	14,678	1,870	12.74%	12,941	1,665	12.87%
Other	29,389	3,091	10.52%	28,187	3,116	11.05%	27,675	3,251	11.75%
	46,346	5,111	11.03%	42,865	4,986	11.63%	40,616	4,916	12.10%
International									
Mortgages and consumer instalment loans	1,079	164	15.20%	768	121	15.76%	785	120	15.29%
Other	18,060	1,713	9.49%	18,083	1,942	10.74%	17,399	1,997	11.48%
	19,139	1,877	9.81%	18,851	2,063	10.94%	18,184	2,117	11.64%
Total loans	65,485	6,988	10.67%	61,716	7,049	11.42%	58,800	7,033	11.96%
Total earning assets	88,835	9,112	10.26%	84,582	9,366	11.07%	79,257	9,239	11.66%
Other Assets	8,875	—	—	7,720		–	7,405	—	—
Total Assets	$97,710	$9,112	9.32%	$92,302	$9,366	10.14%	$86,662	$9,239	10.66%

NET INTEREST INCOME ON AVERAGE ASSETS AND LIABILITIES

(For the year ended October 31)
($ Millions)

	1986			1985			1984		
	Average Balances	*Interest*	*Average Rate*	*Average Balances*	*Interest*	*Average Rate*	*Average Balances*	*Interest*	*Average Rate*
Liabilities									
Interest-Bearing Liabilities									
Deposits									
Domestic									
Demand	$ 5,759	$ 95	1.65%	$ 5,512	$ 105	1.90%	$ 5,916	$ 147	2.48%
Notice	21,714	1,290	5.94%	19,417	1,179	6.07%	16,812	1,118	6.65%
Fixed term	23,030	2,040	8.86%	21,676	2,104	9.71%	21,502	2,107	9.80%
	50,503	3,425	6.78%	46,605	3,388	7.27%	44,230	3,372	7.62%
International									
Demand	1,437	37	2.57%	1,341	30	2.24%	1,322	43	3.25%
Notice	1,459	87	5.96%	1,107	80	7.23%	1,063	95	8.94%
Fixed term	30,777	2,427	7.89%	31,761	3,065	9.65%	29,801	3,095	10.39%
	33,673	2,551	7.58%	34,209	3,175	9.28%	32,186	3,233	10.04%
Total deposits	84,176	5,976	7.10%	80,814	6,563	8.12%	76,416	6,605	8.64%
Liabilities of subsidiaries other than deposits	389	38	9.77%	347	39	11.24%	342	39	11.40%
Bank debentures	1,874	172	9.18%	1,429	148	10.36%	1,115	120	10.76%
Total interest-bearing liabilities	86,439	6,186	7.16%	82,590	6,750	8.17%	77,873	6,764	8.69%
Other Liabilities	6,859	—	—	5,748	—	—	5,260	—	—
Capital & Reserves	4,412	—	—	3,964	—	—	3,529	—	—
Total Liabilities	$97,710	$6,186	6.33%	$92,302	$6,750	7.31%	$86,662	$6,764	7.80%
Total Assets/Net Interest Income	$97,710	$2,926	2.99%	$92,302	$2,616	2.83%	$86,662	$2,475	2.86%

Domestic Highlights – Quarterly

(as a per cent of average assets)

	1986 Q4	1986 Q3	1986 Q2	1986 Q1	1985 Q4	1985 Q3	1985 Q2	1985 Q1
Net interest income (taxable equivalent basis)	3.43%	3.44%	3.33%	3.47%	3.28%	3.31%	3.24%	3.27%
Provision for loan losses	(.75)	(.69)	(.70)	(.63)	(.54)	(.54)	(.63)	(.64)
	2.68	2.75	2.63	2.84	2.74	2.77	2.61	2.63
Other income	1.03	1.08	1.03	.98	1.04	.99	.97	.99
	3.71	3.83	3.66	3.82	3.78	3.76	3.58	3.62
Non-interest expenses	(2.57)	(2.69)	(2.73)	(2.53)	(2.57)	(2.66)	(2.63)	(2.56)
	1.14	1.14	.93	1.29	1.21	1.10	.95	1.06
Income taxes (including taxable equivalent adjustment)	(.56)	(.57)	(.46)	(.67)	(.58)	(.54)	(.44)	(.51)
Return on assets	.58%	.57%	.47%	.62%	.63%	.56%	.51%	.55%
Net income ($ millions)	$ 96	$ 93	$ 73	$ 99	$ 97	$ 85	$ 72	$ 77
Average assets ($ billions)	$66.0	$64.6	$63.4	$62.4	$61.3	$59.4	$57.8	$56.2

International Highlights – Quarterly

(as a per cent of average assets)

	1986 Q4	1986 Q3	1986 Q2	1986 Q1	1985 Q4	1985 Q3	1985 Q2	1985 Q1
Net interest income (taxable equivalent basis)	1.98%	2.03%	2.54%	2.20%	2.17%	2.13%	1.82%	2.15%
Provision for loan losses	(1.19)	(1.13)	(1.10)	(1.02)	(.91)	(.84)	(.80)	(.77)
	.79	.90	1.44	1.18	1.26	1.29	1.02	1.38
Other income	.74	.61	.78	.77	.82	.74	.57	.66
	1.53	1.51	2.22	1.95	2.08	2.03	1.59	2.04
Non-interest expenses	(1.63)	(1.49)	(1.35)	(1.34)	(1.51)	(1.25)	(1.16)	(1.09)
	(.10)	.02	.87	.61	.57	.78	.43	.95
Income taxes (including taxable equivalent adjustment)	.29	.20	(.25)	(.12)	(.15)	(.24)	(.09)	(.37)
Return on assets	.19%	.22%	.62%	.49%	.42%	.54%	.34%	.58%
Net income ($ millions)	$ 15	$ 19	$ 52	$ 42	$ 35	$ 45	$ 28	$ 49
Average assets ($ billions)	$32.7	$33.2	$34.1	$34.1	$32.8	$33.4	$34.4	$33.3

Total Bank Highlights – Quarterly

(as a per cent of average assets)

	1986 Q4	1986 Q3	1986 Q2	1986 Q1	1985 Q4	1985 Q3	1985 Q2	1985 Q1
Net interest income (taxable equivalent basis)	2.95%	2.96%	3.06%	3.02%	2.89%	2.89%	2.71%	2.85%
Provision for loan losses	(.89)	(.84)	(.84)	(.77)	(.67)	(.64)	(.70)	(.69)
	2.06	2.12	2.22	2.25	2.22	2.25	2.01	2.16
Other income	.93	.92	.94	.90	.96	.90	.82	.87
	2.99	3.04	3.16	3.15	3.18	3.15	2.83	3.03
Non-interest expenses	(2.26)	(2.28)	(2.25)	(2.10)	(2.20)	(2.16)	(2.08)	(2.01)
	.73	.76	.91	1.05	.98	.99	.75	1.02
Income taxes (including taxable equivalent adjustment)	(.28)	(.31)	(.38)	(.47)	(.42)	(.44)	(.30)	(.46)
Return on assets	.45%	.45%	.53%	.58%	.56%	.55%	.45%	.56%
Net income ($ millions)	$ 111	$ 112	$ 125	$ 141	$ 132	$ 130	$ 100	$ 126
Average assets ($ billions)	$98.7	$97.8	$97.5	$96.5	$94.1	$92.8	$92.2	$89.5

Earnings per Share – Basic	$0.89	$0.89	$1.05	$1.22	$1.16	$1.14	$0.85	$1.13
– Fully diluted	$0.83	$0.85	$0.96	$1.10	$1.04	$1.04	$0.80	$1.03
Dividends per Share	$0.50	$0.50	$0.50	$0.50	$0.50	$0.50	$0.50	$0.50

Selected Statistical Data

Ten-Year Analytical Review

	1986	1985	1984	1983	1982	1981	1980	1979	1978	1977
Revenue and Expenses as a Per Cent of Average Total Assets										
Average total assets ($ millions)	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Net interest income (taxable equivalent basis) (1)	**2.99%**	2.83%	2.86%	2.80%	2.37%	2.72%	2.82%	2.95%	3.14%	3.04%
Provision for loan losses	**(.84)**	(.67)	(.62)	(.52)	(.39)	(.25)	(.22)	(.23)	(.26)	(.26)
	2.15	2.16	2.24	2.28	1.98	2.47	2.60	2.72	2.88	2.78
Other income	**.93**	.89	.82	.77	.66	.68	.67	.70	.72	.77
	3.08	3.05	3.06	3.05	2.64	3.15	3.27	3.42	3.60	3.55
Non-interest expenses	**(2.22)**	(2.11)	(2.08)	(2.01)	(1.89)	(1.88)	(2.11)	(2.19)	(2.36)	(2.47)
	.86	.94	.98	1.04	.75	1.27	1.16	1.23	1.24	1.08
Income taxes (including taxable equivalent adjustment)	**(.36)**	(.41)	(.46)	(.49)	(.35)	(.61)	(.52)	(.56)	(.53)	(.48)
Minority interests	—	—	—	—	—	(.01)	(.02)	(.04)	(.01)	(.01)
Return on assets	**.50%**	.53%	.52%	.55%	.40%	.65%	.62%	.63%	.70%	.59%
Share Information (2)										
Shares outstanding (thousands) (3)	**106,522**	97,322	90,840	86,769	83,830	81,710	73,402	73,180	73,180	73,180
Earnings per share – Basic	**$4.05**	$4.28	$4.25	$5.03	$3.87	$5.75	$4.74	$3.96	$3.57	$2.57
– Fully diluted	**$3.74**	$3.91	$3.87	$4.58	$3.68	$5.71	$4.74	$3.96	$3.57	$2.57
Dividends	**$2.00**	$2.00	$2.00	$2.00	$2.00	$1.70	$1.26	$1.09	$0.78	$0.69
Common Share price (4) High	**$35.25**	$32.38	$35.38	$36.00	$27.50	$32.25	$27.75	$23.38	$19.00	$14.31
Low	**$27.50**	$27.50	$24.88	$23.50	$18.00	$24.13	$17.94	$16.88	$12.19	$11.38
Close	**$33.25**	$31.50	$28.38	$31.75	$23.50	$25.75	$26.75	$18.69	$17.50	$12.38
Book value (5)	**$34.14**	$33.10	$30.85	$30.05	$29.82	$30.79	$26.86	$23.95	$20.31	$16.93
Price/earnings ratio (6)	**7.7**	7.0	7.1	5.9	5.9	4.9	4.8	5.1	4.4	5.0
Dividend yield (7)	**6.4%**	6.7%	6.6%	6.7%	8.8%	6.0%	5.5%	5.4%	5.0%	5.4%
Return on equity (8)	**12.0%**	13.5%	13.8%	16.8%	12.7%	20.0%	17.8%	17.9%	19.2%	16.1%
Other Information										
Number of shareholders (9)	**89,752**	89,947	79,085	62,332	51,159	47,587	38,463	32,058	31,503	32,276
Number of employees (10)	**38,186**	37,430	38,189	38,687	39,757	38,953	37,034	36,507	35,660	35,335
Number of branches	**1,495**	1,494	1,510	1,536	1,568	1,574	1,592	1,604	1,600	1,595
Number of automated banking machines	**1,170**	898	712	574	392	220	—	—	—	—

Notes to Selected Statistical Data:

(1) These figures have been adjusted to a taxable equivalent basis to recognize income from tax-exempt sources of the following amounts:

	($ Millions)
1977	36
1978	66
1979	198
1980	230
1981	287
1982	331
1983	225
1984	221
1985	175
1986	174

(2) RBC common stock was split 2 for 1 in March 1981 and all earlier figures have been adjusted accordingly.

(3) Weighted daily average of equivalent fully-paid common shares outstanding.

(4) High and low price of common shares traded on the Toronto Stock Exchange during the fiscal year and the closing price on the last trading day of October.

(5) Common shareholders' equity plus appropriations for contingencies divided by common shares outstanding at October 31.

(6) Average of high and low common share price divided by earnings per share.

(7) Dividends per common share divided by the average of high and low share price.

(8) Net income after taxes less preferred share dividends divided by average of monthly common shareholders' equity plus appropriations for contingencies.

(9) Total common shareholders at October 31.

(10) Full time staff on October 31.

Management's Responsibility for Financial Reporting

These financial statements were prepared by the management of The Royal Bank of Canada. While the form of the financial statements and the accounting policies to be followed are prescribed by the Bank Act and related rules issued by the Inspector General of Banks, many amounts must of necessity be based on the best estimates and judgments of management.

In discharging its responsibility for the integrity and fairness of the financial statements and for the accounting systems from which they are derived, management maintains the necessary system of internal controls designed to provide assurance that transactions are authorized, assets are safe-guarded and proper records maintained. These controls include quality standards in hiring and training of employees, written policies and procedures manuals, a written corporate code of conduct and accountability for performance within appropriate and well defined areas of responsibility.

The system of internal controls is further supported by an inspection staff which conducts periodic inspections of all aspects of the Bank's operations. In addition, the Bank's Chief Inspector has full and free access to the Audit Committee of the Board of Directors which oversees management's responsibilities for financial reporting. The Audit Committee is composed entirely of directors who are neither officers nor employees of the Bank.

The Inspector General of Banks, at least once a year, makes such examination and enquiry into the affairs of the Bank as he feels necessary to satisfy himself that the provisions of the Bank Act, having reference to the safety of the depositors and shareholders of the Bank, are being duly observed and that the Bank is in a sound financial condition.

Touche Ross & Co. and Deloitte Haskins & Sells, the independent auditors appointed by the shareholders of the Bank, have examined our financial statements in accordance with generally accepted auditing standards and their report follows. The shareholders' auditors have full and free access to the Audit Committee to discuss their audit and their related findings as to the integrity of the Bank's financial reporting and the adequacy of the system of internal controls.

Allan R. Taylor
Chairman and
Chief Executive Officer

A. H. Michell
Vice-Chairman

Auditors' Report

To the Shareholders, The Royal Bank of Canada

We have examined the consolidated statement of assets and liabilities of The Royal Bank of Canada as at October 31, 1986 and the consolidated statements of income, appropriations for contingencies and changes in shareholders' equity for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the Bank as at October 31, 1986 and the results of its operations for the year then ended in accordance with accounting principles prescribed by the Bank Act applied on a basis consistent with that of the preceding year.

Touche Ross & Co.
Deloitte Haskins & Sells
Chartered Accountants

Montreal, December 1, 1986

Consolidated Statement of Income

(in thousands of dollars)	*Year Ended October 31, 1986*	*Year Ended October 31, 1985*
Interest Income		
Loans	$6,922,343	$6,985,559
Lease financing	65,969	64,012
Securities	855,902	770,747
Deposits with banks	1,093,924	1,371,002
	8,938,138	9,191,320
Interest Expense		
Deposits	5,975,869	6,563,649
Bank debentures	172,297	147,623
Other	37,975	39,133
	6,186,141	6,750,405
Net Interest Income	2,751,997	2,440,915
Provision for loan losses	817,000	621,000
Net Interest Income After Provision for Loan Losses	1,934,997	1,819,915
Other income	904,378	818,541
Net Interest and Other Income	2,839,375	2,638,456
Non-Interest Expenses		
Salaries	1,147,233	1,076,166
Pension and other staff benefits	107,249	104,498
Premises and equipment, including depreciation	377,197	325,676
Other	540,841	441,831
	2,172,520	1,948,171
Net Income Before Income Taxes	666,855	690,285
Income taxes (note 2)	175,000	200,000
Net Income Before Minority Interests	491,855	490,285
Minority interests in subsidiaries	2,965	2,180
Net Income	$ 488,890	$ 488,105
Income per Share (note 3)		
Basic	$4.05	$4.28
Fully diluted	$3.74	$3.91

Consolidated Statement of Assets and Liabilities

(in thousands of dollars)	*October 31, 1986*	*October 31, 1985*
Assets		
Cash Resources		
Cash and deposits with Bank of Canada	**$ 1,385,701**	$ 1,406,259
Deposits with other banks	**13,522,326**	13,585,754
	14,908,027	14,992,013
Securities (note 4)		
Issued or guaranteed by Canada	**3,263,469**	3,731,400
Issued or guaranteed by provinces and municipal or school corporations	**33,845**	158,295
Other securities	**6,946,564**	6,600,534
	10,243,878	10,490,229
Loans (note 5)		
Day, call and short loans to investment dealers and brokers, secured	**971,568**	626,933
Loans to banks	**2,439,163**	2,027,060
Mortgage loans	**13,593,157**	11,036,848
Other loans	**48,930,313**	50,139,962
	65,934,201	63,830,803
Other		
Customers' liability under acceptances	**5,437,753**	4,137,263
Land, buildings and equipment (note 6)	**1,168,247**	1,028,192
Other assets (note 7)	**1,914,459**	1,538,363
	8,520,459	6,703,818
	$99,606,565	$96,016,863

(in thousands of dollars)	*October 31, 1986*	*October 31, 1985*
Liabilities		
Deposits (note 8)		
Payable on demand	**$ 7,280,967**	$ 7,638,391
Payable after notice	**24,979,659**	22,471,630
Payable on a fixed date	**51,992,645**	53,432,948
	84,253,271	83,542,969
Other		
Cheques and other items in transit, net	**333,846**	195,072
Acceptances	**5,437,753**	4,137,263
Liabilities of subsidiaries other than deposits (note 9)	**425,754**	362,369
Other liabilities (note 10)	**2,417,179**	1,853,557
Minority interests in subsidiaries	**9,299**	8,528
	8,623,831	6,556,789
Subordinated Debt		
Bank debentures (note 11)	**2,067,821**	1,749,254
Capital and Reserves		
Appropriations for contingencies	**100,712**	100,712
Shareholders' equity		
Capital stock (note 12)	**2,217,561**	1,839,009
Retained earnings	**2,343,369**	2,228,130
	4,661,642	4,167,851
	$99,606,565	$96,016,863

ALLAN R. TAYLOR
Chairman and Chief Executive Officer

JOHN E. CLEGHORN
President

Consolidated Statement of Appropriations for Contingencies

(in thousands of dollars)	*Year Ended October 31, 1986*	*Year Ended October 31, 1985*
Balance at Beginning of Year (including tax-deductible of $48,409 in 1986; nil in 1985)	**$100,712**	$102,712
Loss experience on loans	**(975,000)**	(685,000)
Provision for loan losses included in the Statement of Income	**817,000**	621,000
Transfer from Retained Earnings	**158,000**	62,000
Balance at End of Year (including tax-deductible of nil in 1986; $48,409 in 1985)	**$100,712**	$100,712

Consolidated Statement of Changes in Shareholders' Equity

(in thousands of dollars)	*Year Ended October 31, 1986*	*Year Ended October 31, 1985*
Capital Stock		
Balance at Beginning of Year	**$1,839,009**	$1,646,751
Issue of preferred shares	**150,000**	—
Issue of common shares	**230,732**	191,458
Preferred shares purchased for cancellation	**(4,510)**	(4,510)
Translation adjustment on shares issued in foreign currency	**2,330**	5,310
Balance at End of Year	**$2,217,561**	$1,839,009
Retained Earnings		
Balance at Beginning of Year	**$2,228,130**	$1,991,772
Net income	**488,890**	488,105
Dividends (note 12)	**(280,758)**	(267,731)
Gain on preferred shares purchased for cancellation	**147**	535
Transfer to Appropriations for Contingencies	**(158,000)**	(62,000)
Income taxes related to the above transfer (note 2)	**86,000**	82,000
Expenses of share issues net of income taxes (note 2)	**(3,100)**	—
Unrealized foreign currency translation losses net of income taxes (note 2)	**(17,940)**	(4,551)
Balance at End of Year	**$2,343,369**	$2,228,130

1. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements of The Royal Bank of Canada are prepared in accordance with accounting principles prescribed by the Bank Act and the related rules issued by the Inspector General of Banks under the authority of the Minister of Finance, and other prevailing practices of the banking industry. These regulations require the Bank to carry its assets and liabilities on the historical cost basis and to follow the accrual method of accounting.

The accounting principles followed in determining Net Income conform in all material respects with accounting principles generally accepted in Canada except for (i) the deferral of gains and losses on the disposal of debt securities, (ii) the accounting for losses on loans and (iii) the translation of foreign currencies.

The significant accounting policies of the Bank are summarized below:

Basis of Consolidation

The consolidated financial statements include the assets and liabilities and results of operations of all subsidiaries after elimination of intercompany transactions and balances. The Bank accounts for the acquisition of subsidiaries using the purchase method; any difference between the cost of the investment and the fair value of assets acquired is amortized over appropriate periods varying from 5 to 25 years.

Investments in associated corporations (corporations owned between 20% and 50%) are accounted for using the equity method. The Bank's share of earnings of these associated corporations and gains and losses realized on dispositions of investments in associated corporations are included in income from securities.

As required by the Bank Act, a listing of subsidiaries, associated corporations and other corporations in which the Bank owns in excess of 10% of the voting shares is shown in note 17; separate condensed Statements of Assets and Liabilities and condensed Statements of Income for Royal Bank Mortgage Corporation, RoyLease Limited and Royal Bank Venture Capital Limited are included in note 16.

Translation of Foreign Currencies

Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates prevailing on the balance sheet date; income and expenses are translated at prevailing quarter-end rates.

Foreign exchange trading positions, including spot and forward contracts, are valued monthly at prevailing market rates and the resulting gains and losses are included in "Other income". Realized gains and losses on foreign exchange transactions are also included in "Other income".

Unrealized foreign currency translation gains and losses (net of hedging gains and losses) on investments in foreign branches, subsidiaries and associated corporations are recorded in Retained Earnings. On disposal of such investments, the accumulated net translation gain or loss is included in income.

Interest Rate Futures

The Bank uses interest rate futures in trading activities and to hedge asset and liability values and interest rate exposure.

When used in trading activities, interest rate futures are marked to market and the resultant gains and losses are recognized in current income.

When used for hedging purposes, gains and losses on interest rate futures are deferred and recognized in income over the average expected remaining life of the hedged asset or liability.

Interest Rate and Cross Currency Swaps

The Bank enters into interest rate and cross currency swaps as an intermediary between swapping counterparties in order to earn fee income, and as a principal in order to manage interest rate and foreign currency exposure.

When acting as an intermediary, the Bank records fees for arrangement services in income as received.

When acting as a principal, the bank accrues income or expense associated with interest rate and cross currency swaps over the life of the agreements.

Foreign Currency Options

The Bank enters into foreign currency options as a writer in order to earn fee income, and as a purchaser in order to manage foreign currency exposure.

Both written and purchased foreign currency options are marked to market and the resultant gains and losses are recognized in current income. For written options, the maximum gain accrued is equal to the premiums received at inception; for purchased options, the maximum loss accrued is equal to the premiums paid at inception.

Securities

Securities comprise investment account and trading account securities as well as loan substitute securities.

Investment account securities are carried at amortized cost. Premiums and discounts are amortized to income on the yield method over the period to maturity of the related securities. Gains and losses realized on disposal of debt securities other than Treasury Bills are deferred and amortized to income over five years. Gains and losses realized on disposal of other investment securities and write-downs to reflect permanent impairment in value are included in income in the period in which they occur.

Trading account securities are carried at estimated current market value. Gains and losses realized on disposal and unrealized valuation adjustments are included in income in the period in which they occur.

Loan substitute securities are accorded the accounting treatment applicable to Loans.

Loans

Loans are stated net of unearned interest and provisions for losses. Specific provisions are established on a loan-by-loan basis to recognize anticipated losses on all types of loans except credit card balances, which are written off when no payment has been received for 180 days. In addition, general provisions are made in respect of overall exposure in a number of troubled countries based on an assessment of the underlying economic conditions in those countries. Aggregate specific provisions and general provisions for losses on loans are increased by new provisions (the "Loss experience on loans") and reduced by loan write-offs net of recoveries. Loans are written off after all reasonable restructuring or collection activities have taken place and the possibility of further recovery is considered to be remote.

The "Loss experience on loans" is charged to "Appropriations for contingencies". The "Provision for loan losses" (based upon a formula prescribed by the Minister of Finance designed to average the loss experience over a five-year period) is charged to income and credited to "Appropriations for contingencies"

Non-performing loans consist of non-accrual loans and renegotiated reduced-rate loans. Non-accrual loans are those placed on a cash basis because there is reasonable doubt regarding the collectibility of principal or interest. Whenever payment of interest is ninety days past due, loans other than credit card balances are automatically placed on a non-accrual basis except in certain instances where management has determined that the collectibility of principal and interest is not reasonably in doubt. Upon classification of a loan to a non-accrual basis any previously accrued but unpaid interest thereon is reversed against income of the current period. In subsequent periods, interest received on non-accrual loans is recorded as income only if management has determined that the loan does not require a specific provision for loss; otherwise interest received is credited to principal. Non-accrual loans are restored to an accrual basis when principal and interest payments are current and there is no longer any reasonable doubt regarding collectibility.

Renegotiated reduced-rate loans provide for a rate of interest lower than the prevailing market rates on similar loans to new borrowers.

Loan fees are included in income as received only where they relate to expenses incurred or services performed. Loan rescheduling fees and fees received which are in lieu of interest are deferred and amortized over the term of the loan.

Lease receivables, included in Loans on the Statement of Assets and Liabilities, represent the aggregate remaining lease payments less unearned income. Unearned income, which at the inception of the lease represents the difference between total lease payments receivable and the cost of the leased asset, is amortized to income over the lease term so as to yield a constant rate of return on the declining balance of the lease receivable.

Acceptances

The Bank's potential liability under acceptances is reported as a liability in the Statement of Assets and Liabilities. The Bank's recourse against the customer in the cáse of a call on these commitments is reported as an offsetting asset of the same amount.

Land, Buildings and Equipment

Land, buildings and equipment are reported at cost and are depreciated principally on the straight-line method over their estimated useful lives as indicated below. Gains and losses on disposal are recorded in income.

Buildings	20 to 50 years
Computer equipment	6 years
Furniture, fixtures and other equipment	7 to 10 years
Leasehold improvements	term of lease plus first option period

Appropriations for Contingencies

The Bank makes appropriations for contingencies with respect to possible unforeseen losses on loans (in addition to specific provisions for losses on identified loans and general provisions for losses on lending to troubled countries) through transfers from Retained Earnings. Of such transfers, the maximum amount which may be made on a tax-deductible basis is prescribed in regulations of the Minister of Finance.

Income Taxes

The Bank follows the tax allocation basis of accounting under which income taxes on specific transactions are recorded in the periods in which the transactions are recognized for accounting purposes regardless of when the transactions are recognized for tax purposes. Income taxes comprise amounts applicable to income included in the Statement of Income, to items charged or credited to Retained Earnings, and to the tax-deductible transfers from Retained Earnings to Appropriations for Contingencies. Deferred income taxes accumulated as a result of timing differences are included either in "Other assets" or "Other liabilities" as applicable. In addition, the Statement of Income contains items which are non-taxable or non-deductible for income tax purposes. Such permanent differences cause the income tax provision to be different than it would be based on statutory rates.

2. Income Taxes

	1986	*1985*
The total income taxes for the year are reported in the consolidated financial statements as follows:		
Statement of Income	**$175,000**	$200,000
Statement of Retained Earnings		
Transfer to appropriations for contingencies	**(86,000)**	(82,000)
Expenses of share issues	**(3,000)**	—
Unrealized foreign currency translation losses	**(54,000)**	(38,000)
Total Income Taxes	**$ 32,000**	$ 80,000
The current and deferred income taxes are as follows:		
Current income taxes	**$ 64,933**	$ 60,385
Deferred income taxes	**(32,933)**	19,615
Total Income Taxes	**$ 32,000**	$ 80,000
Income taxes in the Statement of Income are at an effective rate less than the combined federal and provincial statutory income tax rate for the following reasons:		
Combined federal and provincial statutory income tax rate	**50.4%**	48.9%
Increase (decrease) in rate resulting from:		
Tax-exempt income from securities, primarily income debentures, term preferred shares and small business bonds	**(13.1)**	(13.4)
Lower average tax rate applicable to foreign subsidiaries	**(11.1)**	(7.2)
Other, net	—	0.7
Effective income tax rate	**26.2%**	29.0%

3. Income per Share

Basic Income per Share is after deducting preferred dividends of $75,851,000 (1985 – $71,780,000) and has been calculated on the average number of common shares outstanding. The average number of common shares outstanding for the year ended October 31, 1986 was 102,110,394 (1985 – 97,321,503).

Fully Diluted Income per Share has been calculated on the average number of common shares which would have been outstanding in each year assuming conversion of all convertible securities and exercise of all warrants outstanding as at the beginning of each year or date of issue if later. For purposes of this calculation, adjustments have been made for the after-tax interest on convertible debentures, the dividends on convertible preferred shares and an imputed after-tax return at an appropriate rate on additional funds of $41,997,000 which would be received on the conversion of the second preferred shares series A.

4. Securities

	Maturity					*1986*		*1985*	
	Within 1 Year	*1 to 3 Years*	*3 to 5 Years*	*5 to 10 Years*	*Over 10 Years*	*Carrying Amount*	*Estimated Market Value*	*Carrying Amount*	*Estimated Market Value*
Loan Substitute Securities (1)									
Income debentures	$ 25,291	$ 75,426	$ 14,921	$ 20,862	$ 120,000	**$ 256,500**	**$ 256,500**	$ 318,117	$ 318,117
Small business bonds	4,999	66,069	144,576	—	—	**215,644**	**215,644**	442,281	442,281
Term preferred shares	177,932	603,201	413,750	255,851	22,174	**1,472,908**	**1,472,908**	1,734,034	1,734,034
	208,222	744,696	573,247	276,713	142,174	**1,945,052**	**1,945,052**	2,494,432	2,494,432
Investment Account Securities									
Issued or guaranteed by Canada and provinces	3,088,532	608	96,483	81	1,999	**3,187,703**	**3,186,693**	3,616,257	3,617,641
Other debt	2,117,675	387,334	348,807	369,644	148,696	**3,372,156**	**3,401,948**	2,694,840	2,711,342
Other equity (2)					510,267	**510,267**	**509,527**	462,259	439,935
	5,206,207	387,942	445,290	369,725	660,962	**7,070,126**	**7,098,168**	6,773,356	6,768,918
Trading Account Securities	214,655	45,235	119,759	472,500	222,333	**1,074,482**	**1,074,482**	1,068,744	1,068,744
Securities of Associated Corporations (2)					154,218	**154,218**	**154,218**	153,697	153,697
	$5,629,084	$1,177,873	$1,138,296	$1,118,938	$1,179,687	**$10,243,878**	**$10,271,920**	$10,490,229	$10,485,791

(1) Loan substitute securities have been structured as after-tax instruments rather than conventional loans in order to provide the issuers with a borrowing rate advantage. The securities bear interest at floating rates and are identical in risk and security to bank loans of comparable term.

(2) Securities of associated corporations and other equity securities have no stated term and have been classified under the "over 10 years" column.

5. Loans, net of Provisions for Losses

	1986	1985
Domestic*		
Day, call and short loans to investment dealers and brokers, secured	$ 858,418	$ 577,185
Provinces and municipal or school corporations	182,608	287,072
Lease receivables	526,652	455,634
Consumer instalment loans	5,866,345	5,410,826
Mortgage loans	12,708,717	10,611,365
Other loans	27,757,503	26,997,944
	47,900,243	44,340,026
International*		
Lease receivables	291,784	193,765
Associated corporations	77,216	119,708
Loans to banks	2,284,070	2,024,945
Consumer instalment loans	450,107	431,382
Mortgage loans	884,440	425,483
Other loans	14,046,341	16,295,494
	18,033,958	19,490,777
	$65,934,201	$63,830,803

**Domestic loans include all loans booked in Canada, regardless of currency, with the exception of those of the Canadian-based International Money Markets. The loans of this unit, together with loans booked outside Canada, comprise International loans.*

Non-Performing Loans, net of Provisions for Losses (included above)

	1986	1985
Non-accrual Loans		
Domestic	$1,566,998	$1,231,205
International	726,814	1,217,892
	$2,293,812	$2,449,097
Renegotiated Reduced-Rate Loans		
Domestic	$70,639	$174,593
International	6,473	5,337
	$77,112	$179,930

6. Land, Buildings and Equipment

	Cost	Accumulated Depreciation	1986 Net Book Value	1985 Net Book Value
Land	$ 135,953	$ –	$ 135,953	$ 130,112
Buildings	710,358	158,190	552,168	475,968
Computer equipment	386,011	180,603	205,408	171,738
Furniture, fixtures and other equipment	387,257	252,926	134,331	122,950
Leasehold improvements	235,185	94,798	140,387	127,424
	$1,854,764	$686,517	$1,168,247	$1,028,192

Depreciation expense for the year ended October 31, 1986 was $116,189,000 (1985 – $97,867,000)

7. Other Assets

	1986	1985
Accrued interest	$ 803,454	$ 972,796
Deferred pension costs	50,349	42,200
Deferred income taxes	95,912	60,388
Goodwill	62,886	54,542
Other items, including accounts receivable and prepaid expenses	901,858	408,437
	$1,914,459	$1,538,363

8. Deposits

	Payable on Demand	Payable after Notice	Payable on a Fixed Date	1986 Total	1985 Total
Domestic*					
Deposits by Canada	$ 149,054	$ —	$ 300,000	$ 449,054	$ 1,295,651
Deposits by provinces	50,837	9,377	33,539	93,753	57,105
Deposits by banks	571,311	35,474	177,466	784,251	575,107
Deposits by individuals	867,835	19,932,764	16,159,348	36,959,947	34,862,080
Other deposits	4,317,126	3,394,083	5,457,521	13,168,730	12,764,946
	5,956,163	23,371,698	22,127,874	51,455,735	49,554,889
International*					
Deposits by provinces	—	—	113,605	113,605	81,422
Deposits by banks	162,806	440,768	15,831,448	16,435,022	18,356,649
Deposits by individuals	392,296	945,909	2,732,508	4,070,713	4,091,493
Other deposits	769,702	221,284	11,187,210	12,178,196	11,458,516
	1,324,804	1,607,961	29,864,771	32,797,536	33,988,080
	$7,280,967	$24,979,659	$51,992,645	$84,253,271	$83,542,969

**Domestic deposits include all deposits booked in Canada, regardless of currency, with the exception of those of the Canadian-based International Money Markets. The deposits of this unit, together with deposits booked outside Canada, comprise International deposits.*

9. Liabilities of Subsidiaries Other Than Deposits

These liabilities are subordinated in right of payment to claims of the depositors and certain other creditors of the respective subsidiaries.

	1986	1985
RoyLease Limited		
Long-term notes payable in various amounts to 1992 and bearing interest at rates from 5¾% to 13¼%	$350,034	$298,901
The Royal Bank of Canada International Limited		
7¾% DM 100,000,000 bonds due 1990	52,777	52,255
Other subsidiaries	22,943	11,213
	$425,754	$362,369

10. Other Liabilities

	1986	1985
Accrued interest	$1,198,711	$1,210,393
Dividends payable	70,112	67,302
Unamortized gains on disposal of debt securities	65,778	53,513
Other items, including accounts payable and accrued expenses	1,082,578	522,349
	$2,417,179	$1,853,557

11. Bank Debentures

The debentures are direct unsecured obligations of the Bank and are subordinated in right of payment to the claims of depositors and certain other creditors of the Bank.

In accordance with the formula prescribed in the Bank Act, as at November 1, 1986 the Bank had the capacity to issue an additional $425,000,000 of debentures.

Maturity	*Rate*			*1986*	*1985*
May 15, 1986	10%			$ —	$ 40,000
June 1, 1986	9¼%			—	60,000
April 7, 1987		(2)		**139,080**	136,750
June 1, 1987	9%			**75,000**	75,000
December 1, 1987	7½%	(1)	Callable	**789**	789
April 1, 1988	9½%	(1)	Callable	**16,854**	19,803
February 15, 1989	10.40%			**75,000**	75,000
November 15, 1990		(3)		**75,000**	75,000
April 15, 1991	7%	(1)	Callable	**2,762**	2,762
July 22, 1991	12%	(4)	Convertible	**100,000**	100,000
December 9, 1991	11¼%	(5)	Convertible, callable on or after December 10, 1986	**259,629**	259,778
February 15, 1992	9%	(1)	Callable	**31,347**	31,547
May 15, 1994	10%	(1)	Callable	**34,141**	34,908
December 1, 1994	10%	(1)	Callable	**6,669**	6,729
May 22, 2000	11⅝%	(1),(6)	Callable on or after November 22, 1992	**97,530**	102,562
July 5, 2005		(7)	Callable on or after July 6, 1990	**486,780**	478,626
October 1, 2083		(8)	Callable on or after October 2, 1989	**250,000**	250,000
June 6, 2085		(9)	Callable on or after June 6, 1991	**417,240**	—
				$2,067,821	$1,749,254

(1) Subject to sinking fund provisions.

(2) The April 7, 1987 debentures are denominated in U.S. dollars and are carried at the Canadian equivalent of U.S.$100,000,000. These debentures bear interest at a rate equal to the average of the six months LIBOR.

(3) The November 15, 1990 debentures bear interest at a rate of ⅜ of 1% below the Bank's average Canadian prime rate.

(4) The July 22, 1991 debentures are convertible at the option of the holder up to and including July 21, 1991 into Common Shares at a conversion price of $35 per Common Share. These debentures are also convertible at the option of the Bank at a conversion price of $35 per Common Share if the Common Shares have traded at or in excess of certain weighted average prices.

(5) Subject to the call provisions, the December 9, 1991 debentures are convertible at the option of the holder up to and including December 9, 1991 into Common Shares at a conversion price of $30 per Common Share subject to adjustment in certain events.

(6) The May 22, 2000 debentures are denominated in U.S. dollars and are carried at the Canadian equivalent of U.S.$70,125,000.

(7) The July 5, 2005 debentures are denominated in U.S. dollars and are carried at the Canadian equivalent of U.S. $350,000,000. These debentures bear interest at a rate of 1/16 of 1% above LIBOR.

(8) The October 1, 2083 debentures bear interest at a rate of .40% above the 30-day Bankers' Acceptance rate reported by the Bank of Canada.

(9) The June 6, 2085 debentures are denominated in U.S. dollars and are carried at the Canadian equivalent of U.S. $300,000,000. These debentures bear interest at a rate equal to ¼ of 1% above the average of the three months LIBOR. In the event of a reduction of the annual dividend declared by the Bank on its Common Shares, the interest payable on the debentures is reduced pro-rata to the dividend reduction and the interest reduction is payable with the proceeds from the sale of Common Shares.

The aggregate sinking fund requirements and maturities of the Bank's debentures assuming the earliest possible dates of maturity under the terms of issue are as follows:

Within 1 year	$ 230,348
From 1 to 2 years	24,409
From 2 to 3 years	84,620
From 3 to 5 years	197,002
From 5 to 10 years	349,611
Over 10 years	1,181,831
	$2,067,821

12. Capital Stock

Authorized Capital Stock

Preferred – 50,000,000 First Preferred Shares and 50,000,000 Second Preferred Shares without nominal or par value, issuable in series; the aggregate consideration for which all the First Preferred Shares and all the Second Preferred Shares may be issued shall not exceed $1,250,000,000 in each case.

Common – 250,000,000 shares without nominal or par value provided that the aggregate consideration shall not exceed $3,000,000,000.

	1986		1985	
Outstanding Capital Stock	*Number of Shares (in thousands)*	*Amount*	*Number of Shares (in thousands)*	*Amount*
First Preferred				
$1.88 Cumulative Redeemable First Preferred Shares Series A (1)				
Outstanding at beginning of year	5,205	$130,133	5,386	$ 134,643
Purchased for cancellation	180	4,510	181	4,510
Outstanding at end of year	5,025	125,623	5,205	130,133
$1.45 First Preferred Shares Series B, Cumulative and Redeemable and Convertible when tendered with Common Share Warrants (2)				
Outstanding at end of year	15,000	300,000	15,000	300,000
Floating Rate Cumulative Redeemable First Preferred Shares Series C (3)				
Outstanding at end of year	1,000	100,000	1,000	100,000
U.S.$ Floating Rate Cumulative Redeemable First Preferred Shares Series D (3)				
Outstanding at beginning of year	1,000	136,750	1,000	131,440
Foreign currency translation adjustment		2,330		5,310
Outstanding at end of year	1,000	139,080	1,000	136,750
Price Adjusted Floating Rate Cumulative Redeemable First Preferred Shares Series E (4)				
Issued in April 1986 and outstanding at end of year	1,500	150,000	—	—
Second Preferred				
$2.75 Cumulative Redeemable Convertible Second Preferred Shares Series A (5)				
Outstanding at end of year	8,399	209,985	8,399	209,985
Common				
Outstanding at beginning of year	99,427	962,141	92,873	770,683
Issued monthly under the Shareholder Dividend and Share Purchase Plan	4,090	128,583	6,554	191,455
Issued in October 1986	3,000	102,000	—	—
Issued on conversion of Debentures	5	149	—	3
Outstanding at end of year	106,522	1,192,873	99,427	962,141
Total Outstanding Capital Stock		$2,217,561		$1,839,009

(1) The Bank has undertaken to purchase in each calendar quarter 48,000 of the First Preferred Shares Series A, if available, at prices not exceeding $25 per share.

(2) 7,500,000 Common Share Warrants are outstanding. Each Warrant entitles the holder to purchase one Common Share at a price of $40 on or prior to June 9, 1988, subject to adjustment in certain events. In addition, each Warrant gives the holder the option to tender two First Preferred Shares Series B, in lieu of cash, in return for one Common Share, subject to adjustment in certain events. After June 9, 1988 the Bank will have the option to redeem the First Preferred Shares Series B at $21 per share reducing by $0.20 per year until June 9, 1993 and thereafter at $20. The Bank may at any time purchase for cancellation First Preferred Shares Series B at a price per share, if purchased at any time on or prior to June 9, 1988, not exceeding $21 and, if purchased thereafter, at a price per share not exceeding the then applicable above-mentioned redemption price. These redemption and purchase for cancellation options are subject to the consent of the Inspector General of Banks.

(3) The dividends on the First Preferred Shares Series C and D are determined quarterly by applying to Cdn.$100 and U.S.$100 respectively, the greater of (i) 6.67% per annum and (ii) $^2/_3$ of the Bank's average Canadian and U.S. prime rates respectively for stated periods. The First Preferred Shares Series C and D are not redeemable by the Bank prior to June 8, 1989 but thereafter are redeemable at a price per share of Cdn.$100 and U.S.$100 respectively. The Bank may at any time purchase for cancellation First Preferred Shares Series C and D at a price per share, not exceeding Cdn.$100 and U.S.$100 respectively. These redemption and purchase for cancellation options are subject to the consent of the Inspector General of Banks.

(4) The dividend on the First Preferred Shares Series E is determined monthly and (i) floats in relation to changes in the Bank's average Canadian prime rate, and (ii) is adjusted upwards or downwards based on changes in market trading value. The annual dividend rate applicable to any month will in no event be less than 55%, or greater than 75% of the average prime rate. The First Preferred Shares Series E are not redeemable by the Bank prior to April 30, 1991 but thereafter are redeemable at a price per share of $100. The Bank may at any time purchase for cancellation First Preferred Shares Series E at a price per share not exceeding $100. These redemption and purchase for cancellation options are subject to the consent of the Inspector General of Banks.

(5) Subject to the Bank's right of conversion, each Second Preferred Share Series A is convertible at the option of the holder up to and including December 8, 1988 into one Common Share upon payment by the holder of $5, being a conversion price of $30 per Common Share, subject to adjustment in certain events. If the Common Shares trade at a price in excess of 125% of the prevailing conversion price for a specified period, the Bank shall have the right, upon notice, to convert the Second Preferred Shares Series A into Common Shares at the prevailing conversion price. No additional payment will be required from the holders of Second Preferred Shares Series A so converted. However, during the notice period, a holder of Second Preferred Shares Series A will continue to have the right to convert, at his option, each Second Preferred Share Series A into one Common Share upon the payment of $5 per share converted. Commencing January 1, 1989 the Bank has undertaken to purchase in each calendar quarter 1% of the shares outstanding as of December 10, 1988, if available, at prices not exceeding $25 per share. The Second Preferred Shares Series A are retractable at the option of the holder on or before November 9, 1988, for redemption on December 9, 1988 at a price of $28.75 per share.

As at October 31, 1986, Common Shares were reserved for possible issuance as follows:	*Number (in thousands)*
– Under the Shareholder Dividend and Share Purchase Plan	8,820
– Upon conversion of the July 22, 1991 debentures	2,857
– Upon conversion of the December 9, 1991 debentures	8,654
– Upon conversion of the Second Preferred Shares Series A	8,399
– Upon exercise of the Common Share Warrants	7,500
	36,230

Dividends Declared	*1986*	*1985*
Preferred		
First Preferred		
Series A	**$ 9,596**	$ 9,946
Series B	**21,750**	21,750
Series C	**7,102**	7,448
Series D	**9,433**	9,536
Series E	**4,872**	—
Second Preferred		
Series A	**23,098**	23,100
	75,851	71,780
Common	**204,907**	195,951
	$280,758	$267,731

13. Pension Plan

The Bank maintains a defined benefit pension plan which is available to all employees after five years service or at age 25, on a contributory or a non-contributory basis. The plan provides pensions based on years of service, years of contribution, and final average earnings.

An actuarial valuation is performed each year to determine the present value of the accrued pension benefits, based on projections of employees' compensation levels to the time of retirement. Pension fund assets are carried at adjusted market values. As at January 1, 1986, the date of the latest valuation, the pension plan had a funding excess as shown below:

	1986	*1985*
Pension fund assets, at adjusted market values	**$1,127,170**	$998,605
Present value of accrued pension benefits	**900,964**	844,019
Funding excess, as at January 1	**$ 226,206**	$154,586

Effective November 1, 1985 in accordance with new recommendations of the Canadian Institute of Chartered Accountants, the Bank changed its accounting policy with respect to the determination of pension expense. In previous years, pension expense consisted of the amortization of past service pension contributions plus the amount of any funding in respect of current service. Commencing this year, pension expense consists of the aggregate of (a) the actuarially computed cost of pension benefits provided in respect of the current year's service, (b) imputed interest on the funding excess or deficiency and (c) the amortization over the expected average remaining service life of employees of (i) the unamortized past service pension contribution existing as at October 31, 1985, (ii) the funding excess or deficiency existing as at the date of the latest actuarial valuation and (iii) any experience gain or loss during the year. This change in accounting policy has not been applied retroactively and has had the effect of reducing pension expense for the current year by approximately $14 million.

Pension expense amounted to a credit of $1,346,000 for the year ended October 31, 1986 (1985 – expense of $12,013,000).

The cumulative difference between the funding contributions and the amounts recorded as pension expense is reflected in "Other assets".

14. Commitments and Contingent Liabilities

In the normal course of business the Bank undertakes various commitments and has contingent liabilities which are not reflected in the financial statements. These include guarantees and letters of credit, commitments to extend credit, foreign exchange forward contracts, interest rate futures, forward rate agreements, interest rate and cross currency swaps and foreign currency options written. Management does not anticipate any material losses to result from these transactions.

Outstanding amounts in respect of guarantees and letters of credit, including those to associated corporations of $47,833,000 as at October 31, 1986 (1985 – $19,948,000), are as follows:

	1986	*1985*
Guarantees	$3,257,851	$2,940,279
Letters of credit	2,292,869	1,868,193
	$5,550,720	$4,808,472

Minimum future rental commitments for buildings under long-term non-cancellable leases for the next five years are:

1987	$74,116
1988	63,044
1989	55,148
1990	50,016
1991	42,683

Annual rental commitments after 1991 are in decreasing amounts.

Various legal proceedings are pending against the Bank and its subsidiaries. Management considers that the aggregate liability resulting from these proceedings will not be material.

15. Domestic and International Operations

The Bank considers its Domestic Operations to include all business transacted in Canada, regardless of currency, with the exception of the Canadian-based activities of International Money Markets. This unit, together with the Bank's business carried on outside Canada, comprise International Operations. While it is not practicable to make a definitive division of its Domestic and International Operations, appropriate allocations are made for (a) the cost of funds related to liquidity and capital computed on the basis of marginal costs of funds, and (b) corporate non-interest expenses.

	Domestic		*International*		*Total*	
	1986	*1985*	*1986*	*1985*	*1986*	*1985*
Net interest income – taxable equivalent basis	$ 2,192,076	$ 1,922,837	$ 733,740	$ 693,065	$ 2,925,816	$ 2,615,902
Deduct: Taxable equivalent adjustment*	147,057	138,193	26,762	36,794	173,819	174,987
Net interest income – financial statement basis	2,045,019	1,784,644	706,978	656,271	2,751,997	2,440,915
Provision for loan losses	445,000	343,000	372,000	278,000	817,000	621,000
	1,600,019	1,441,644	334,978	378,271	1,934,997	1,819,915
Other income	660,765	584,973	243,613	233,568	904,378	818,541
	2,260,784	2,026,617	578,591	611,839	2,839,375	2,638,456
Non-interest expenses	1,685,854	1,529,183	486,666	418,988	2,172,520	1,948,171
	574,930	497,434	91,925	192,851	666,855	690,285
Income taxes	214,500	166,500	(39,500)	33,500	175,000	200,000
	360,430	330,934	131,425	159,351	491,855	490,285
Minority interests	—	—	2,965	2,180	2,965	2,180
Net income	$ 360,430	$ 330,934	$ 128,460	$ 157,171	$ 488,890	$ 488,105
Average total assets	$64,000,000	$58,800,000	$33,700,000	$33,500,000	$97,700,000	$92,300,000

**The taxable equivalent adjustment represents a credit to interest income in order to gross up the tax-exempt income earned on certain securities (primarily small business bonds, income debentures and term preferred shares) to an amount which, had it been taxable at a rate of 50.4% in 1986 and 48.9% in 1985, would result in the same after tax net income as appears in the financial statements. The gross up of such income to a taxable equivalent basis permits a uniform measurement and comparison of net interest income.*

16. Condensed Financial Statements of Wholly-owned Mortgage, Leasing and Venture Capital Subsidiaries

Royal Bank Mortgage Corporation

Statement of Assets and Liabilities
(in thousands of dollars)

	October 31, 1986	*October 31, 1985*
Assets		
Mortgage loans	$7,108,930	$6,367,515
Personal loans	967,299	987,497
Other investments	486,653	562,419
	$8,562,882	$7,917,431
Liabilities		
Accrued interest and other liabilities	$ 211,648	$ 182,509
The Royal Bank of Canada	1,946,444	3,012,013
Short-term promissory notes	676,563	135,276
Investment certificates		
Due within one year	2,747,682	2,520,386
Due beyond one year	2,635,446	1,745,385
Deferred income taxes	24,604	25,678
Preferred and common stock	125,657	122,800
Contributed surplus	152,143	130,000
Retained earnings	42,695	43,384
	$8,562,882	$7,917,431

Statement of Income
(in thousands of dollars)

	Year Ended *October 31, 1986*	Year Ended *October 31, 1985*
Income		
Interest on mortgages	$673,636	$629,875
Interest on personal loans	74,541	11,692
Interest on investments	50,907	53,273
	799,084	694,840
Expenses		
Interest – The Royal Bank of Canada	160,004	101,318
Interest on short-term promissory notes	66,269	46,236
Interest on investment certificates	483,800	477,761
Operating expenses	78,039	56,412
	788,112	681,727
Net Income Before Income Taxes	10,972	13,113
Income taxes	(1,074)	(5,168)
Net Income	$ 12,046	$ 18,281

RoyLease Limited

Statement of Assets and Liabilities
(in thousands of dollars)

	October 31, 1986	*October 31, 1985*
Assets		
Receivable under lease agreements	$619,650	$552,283
Other	4,894	6,916
	$624,544	$559,199
Liabilities		
Accrued interest and other liabilities	$ 28,002	$ 24,135
Short-term promissory notes	92,439	86,330
Long-term debt		
The Royal Bank of Canada	3,300	3,575
Other	354,834	306,543
Deferred income taxes	82,946	75,924
Common stock	21,975	21,975
Retained earnings	41,048	40,717
	$624,544	$559,199

Statement of Income
(in thousands of dollars)

	Year Ended October 31, 1986	*Year Ended October 31, 1985*
Income		
Leases	$70,903	$68,430
Expenses		
Interest on short-term promissory notes	5,347	5,958
Interest on long-term debt		
The Royal Bank of Canada	1,769	1,672
Other	33,378	30,238
Operating expenses	9,829	11,547
	50,323	49,415
Net Income Before Income Taxes	20,580	19,015
Income taxes	10,249	9,184
Net Income	$10,331	$ 9,831

Royal Bank Venture Capital Limited

Statement of Assets and Liabilities
(in thousands of dollars)

	October 31, 1986	*October 31, 1985*
Assets		
Cash and short-term deposits	$ 50	$ 9
Investments	14,053	10,054
Other assets	242	233
	$14,345	$10,296
Liabilities		
Accrued interest and other liabilities	$ 416	$ 497
The Royal Bank of Canada	8,879	6,315
Common stock	5,669	3,905
Deficit	(619)	(421)
	$14,345	$10,296

Statement of Income
(in thousands of dollars)

	Year Ended October 31, 1986	*Year Ended October 31, 1985*
Income		
Interest and dividends	$ 649	$ 613
Fees and commissions	234	152
Other	211	—
	1,094	765
Expenses		
Interest – The Royal Bank of Canada	669	497
Operating Expenses	623	666
	1,292	1,163
Net Loss Before Income Taxes	(198)	(398)
Income taxes	—	—
Net Loss	$(198)	$(398)

17. Corporations in which the Bank owns more than 10% of the Voting Shares

17. Corporations in which the Bank owns more than 10% of the Voting Shares	*Principal Office Address*	*Carrying Value of Voting Shares owned by the Bank**	*Percent of Voting Shares owned by the Bank*
Royal Bank Mortgage Corporation	Montreal, Canada	$222,495	100%
RoyLease Limited	Montreal, Canada	64,377	100
Royal Bank Realty Inc.	Montreal, Canada	33,726	100
Globe Realty Management Limited	Toronto, Canada		100
Royal Bank Export Finance Co. Ltd.	Toronto, Canada	4,690	100
Royal Bank Venture Capital Limited	Toronto, Canada	5,050	100
RoyNat Inc.	Montreal, Canada	29,339	42
Chargex Ltd.	Montreal, Canada		25
RBC Holdings (USA) Inc.	New York, U.S.A.	180,218	100
The Royal Bank and Trust Company	New York, U.S.A.		100
Orion Royal Inc.	New York, U.S.A.		100
RBC Holdings (Delaware) Inc.	Wilmington, U.S.A.		100
RBC Systems (USA) Inc.	Jersey City, U.S.A.		100
Royal Bank de Puerto Rico	San Juan, Puerto Rico	49,214	100
The Royal Bank of Canada (Middle East) S.A.L.	Beirut, Lebanon	357	55
RBC Australia Holdings Limited	Sydney, Australia	60,518	100
National Mutual Royal Bank Limited	Melbourne, Australia		50
RBC Australia Finance Limited	Sydney, Australia		50
RoyAust Management Limited	Sydney, Australia		50
Capel Court Corporation Limited	Melbourne, Australia		50
National Mutual Royal Savings Bank Limited	Melbourne, Australia		50
The Royal Bank of Canada (Asia) Limited	Singapore	133,400	100
The Royal Bank of Canada Representacoes S/C Ltda.	São Paulo, Brazil	1,738	100
Royal Bank (Barbados) Financial Corporation	Bridgetown, Barbados	779	100
R.B.C. Bay Street Properties Limited	Nassau, Bahamas	33	100
R.B.C. Bahamas Limited	Nassau, Bahamas	675,670	100
Favourable Investments Inc.	Hong Kong		25
Canadian Overseas Development Company Limited	Hong Kong		25
The Royal Bank of Canada International Limited	Nassau, Bahamas		100
Canada International (Cayman) Limited	George Town, Grand Cayman		100
R.B.C. Investments Limited	Nassau, Bahamas		100
RoyWest Holdings Limited	Nassau, Bahamas		50
RoyWest Investments Limited	Nassau, Bahamas		50
RoyWest Trust Corporation Limited	Nassau, Bahamas		50
Finance Corporation of Bahamas Limited	Nassau, Bahamas		75
The Royal Bank of Canada (Barbados) Limited	Bridgetown, Barbados		100
RoyMidEast Limited	George Town, Grand Cayman		100
RoyCan International Banking Limited	Nassau, Bahamas		100
Bishops International Bank Limited	Nassau, Bahamas		100
China Investment and Finance Limited	Hong Kong		50
Banco Royal Colombiano	Bogotá, Colombia	3,156	49
The Royal Bank of Trinidad and Tobago Limited	Port of Spain, Trinidad	26,945	47
Royal Bank Trust Company (Trinidad) Limited	Port of Spain, Trinidad		47
The Royal Bank Mortgage and Finance Company Limited	Port of Spain, Trinidad		47
General Finance Corporation Limited	Port of Spain, Trinidad		19
Banco Royal do Canada (Brasil) S.A.	São Paulo, Brazil	36,885	100
Ouvidor Industria E Comercio Ltda.	Rio de Janeiro, Brazil	6	100
RBC Houdstermaatschappij, B.V.	Amsterdam, Netherlands	16,445	100
The Royal Bank of Canada (France)	Paris, France		100
RBC Finance B.V.	Amsterdam, Netherlands	101,844	100

**The carrying value of voting shares owned 20% or more by the Bank is stated at the Bank's equity in such investments.*

17. CORPORATIONS IN WHICH THE BANK OWNS MORE THAN 10% OF THE VOTING SHARES *(continued)*	*Principal Office Address*	*Carrying Value of Voting Shares owned by the Bank*	*Percent of Voting Shares owned by the Bank*
Multinational Orion Leasing Holdings N.V.	Amsterdam, Netherlands	$ 6,874	100%
Orion Export Leasing Limited	George Town, Grand Cayman		100
Orion Leasing Nederland B.V.	Amsterdam, Netherlands		100
Orion Leasing Singapore Pte. Limited	Singapore		100
RBC Management Services B.V.	Amsterdam, Netherlands	3,034	100
Orion Multinational Services Limited	London, England		100
Orion Multinational Services Inc.	New York, U.S.A.		100
RBC Holdings B.V.	Amsterdam, Netherlands	351,500	100
Orpac Holdings Limited	Hong Kong		100
The Royal Bank of Canada (Suisse)	Geneva, Switzerland		100
The Royal Bank of Canada A.G.	Frankfurt, Germany		100
Intercontact GMBH	Düsseldorf, Germany		100
The Royal Bank of Canada (Belgium) S.A.	Brussels, Belgium		100
The Royal Bank of Canada (Channel Islands) Limited	Guernsey, Channel Islands		100
Orion Royal Bank (Guernsey) Limited	Guernsey, Channel Islands		100
RBC Offshore Fund Managers Limited	Guernsey, Channel Islands		100
The Royal Bank of Canada Trustees (Jersey) Limited	Jersey, Channel Islands		100
The Royal Bank of Canada Trustees (Guernsey) Limited	Guernsey, Channel Islands		100
The Royal Bank of Canada Trust Company (Asia) Limited	Hong Kong		100
RoyCan Trust Company, S.A.	Geneva, Switzerland		100
InchRoy Credit Corporation Limited	Hong Kong		70
The Royal Bank of Canada Holdings (U.K.) Limited	London, England		100
Libra Bank Limited	London, England		11
The Royal Bank of Canada Trade Finance Limited	London, England		100
RBC Trade Finance Serviços Ltda.	São Paulo, Brazil		100
RBC Trade Finance Inc.	New York, U.S.A.		100
RBC Trade Finance S.A.	Brussels, Belgium		100
The Royal Bank of Canada Forfait Finance Limited	London, England		100
The Royal Bank of Canada Trade Credit Limited	London, England		100
The Royal Bank of Canada Export Credit Limited	London, England		100
Tennant-OFE S.A.	Paris, France		70
RBC Properties (U.K.) Limited	London, England		100
Chancellor Investments Limited	London, England		100
Orion Royal Bank Limited	London, England		100
Orion Cayman Limited	George Town, Grand Cayman		100
Orion Royal Bank Equities of Canada Limited	London, England		100
Orion Royal Bank Asset Management Limited	London, England		100
Orion Royal Bank Trust Managers Limited	London, England		100
RBC Gilts Limited	London, England		100
Orion Royal Bank Participations Limited	London, England		100
Kitcat & Aitken & Co.	London, England		100
Orion Leasing Holdings Limited	London, England		100
Orion Leasing Limited	London, England		100
Orion Factors Limited	London, England		100
Orion Finance Limited	London, England		100
Orion Pacific Holdings Limited	Hong Kong		100
Orion Royal Pacific Limited	Hong Kong		100
Orion Caribbean Limited	George Town, Grand Cayman		100
Orion Royal Securities (HK) Limited	Hong Kong		100
RBC Systems Limited	London, England		100
Western Trust & Savings Holdings Limited	Plymouth, England		100
Western Trust & Savings Insurance Services Limited	Plymouth, England		100
Western Trust & Savings Limited	Plymouth, England		100

When he retired May 31, 1986, Rowland C. Frazee had been Chief Executive Officer of the Bank for seven and a half years, and Chairman for almost six years. He piloted Canada's leading financial institution through one of the most turbulent periods in its history, when the economy was assailed by severe inflation, soaring interest rates and the worst recession in 50 years.

That the Bank has emerged in a fundamentally sound position and with a clear business strategy is testimony to Mr. Frazee's remarkable leadership abilities. In the midst of economic turmoil, he steadfastly insisted that we look to the environment and markets of the 1990s and beyond, while also holding the Bank firmly on course from quarter to quarter.

Mr. Frazee presided over the management team while it decided on major investments which have permitted us to seize the lead in electronic banking and to carve out a major place for the Royal in international investment banking. Through his personal example, he instilled a sense of teamwork in the people with whom he worked. He placed strong emphasis on building depth, responsiveness and continuity in management and throughout the Bank. All these achievements reflected his firm commitment to strategic thinking, in the broadest sense of the word.

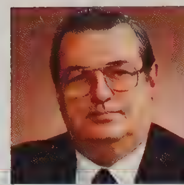
While he was at the helm of the Royal Bank, Rowland Frazee played a statesman's role for the Canadian banking industry as a whole, and made constructive contributions to debates on public policy. Concern for the public interest was one of the pillars of his management philosophy—a principle we in the present management team intend to stick to. We are grateful to Mr. Frazee for giving us such a solid base on which to build the future of the Bank.

A. R. Taylor
Chairman & Chief Executive Officer

Directors

As at October 31, 1986

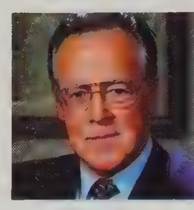
Allan R. Taylor
Toronto
Chairman and Chief Executive Officer
The Royal Bank of Canada



A. H. Michell
Montreal
Vice-Chairman
The Royal Bank of Canada

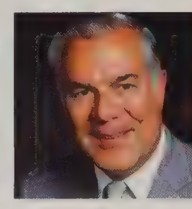
R. G. P. Styles
Toronto
Vice-Chairman
The Royal Bank of Canada

Robin W. Adam
London, England
Chairman
MEPC plc



John Anderson
Vancouver
President and Chief Executive Officer
Westcoast Transmission Company Limited

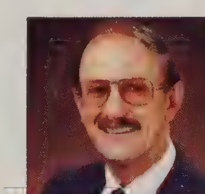
John A. Armstrong
Toronto
Company Director



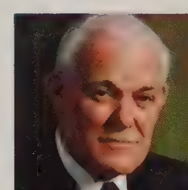
Ian A. Barclay
Vancouver
Chairman
Canada Harbour Place Corporation

G. H. Blumenauer
Oakville
Chairman of the Board
Otis Canada, Inc.

Robert W. Campbell
Calgary
Chairman
Canadian Pacific Limited



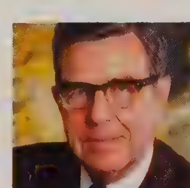
Robert M. Chipman
Winnipeg
Chairman
The Megill-Stephenson Company Limited



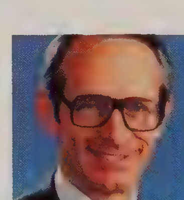
Frank B. Common, Jr., Q.C.
Montreal
Counsel
Ogilvy, Renault

Camille A. Dagenais, C.C., LL.D.
Montreal
Director
The SNC Group

Mitzi S. Dobrin
Montreal
Chairman and Chief Executive Officer
DBRN Holdings Ltd.



G. Campbell Eaton, O.C., M.C., C.D., LL.D.
St. John's, Nfld.
President
Dublin Ltd.



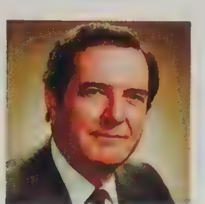
John R. Evans, C.C., M.D.
Mississauga
Chairman and Chief Executive Officer
Allelix Inc.

Jock K. Finlayson
Montreal
Chairman
Royal Insurance
Company of Canada

L. Yves Fortier, O.C., Q.C.
Montreal
Senior Partner
Ogilvy, Renault

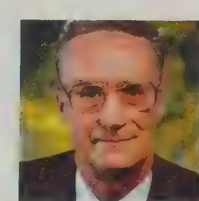
Rowland C. Frazee
Montreal
Retired Chairman
The Royal Bank of
Canada

W. D. H. Gardiner
Vancouver
President
W.D.H.G.
Financial Associates
Ltd.



Arden R. Haynes
Toronto
Chairman, President and Chief Executive Officer
Imperial Oil Limited

Charles H. Knight
Regina
Chief Executive Officer
Denro Holdings
Ltd.



Walter F. Light
Toronto
Retired Chairman
Northern Telecom
Limited

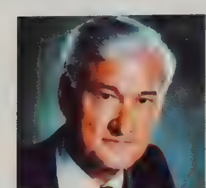
The Hon. E. Peter Lougheed, P.C., Q.C.
Calgary
Senior Partner
Bennett Jones

P. L. P. Macdonnell, C.M., Q.C.
Edmonton
Partner
Milner & Steer

Clifford S. Malone
Toronto
Vice-Chairman
United Corporations
Limited

Alexander B. Marshall
London, England
Chairman
Commercial Union
Assurance Company
plc

J. Pierre Maurer
New York
Vice-Chairman of the Board
Metropolitan Life
Insurance Company



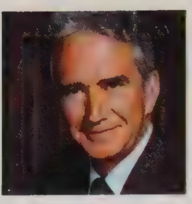
G. Wallace F. McCain
Florenceville, N.B.
President
McCain Foods
Limited

Donald K. McIvor**
New York
Senior Vice-President & Director
Exxon Corporation

Dawn R. McKeag
Winnipeg
President
Walford
Investments Ltd.

W. Earle McLaughlin
Montreal
Former Chairman of the Board
The Royal Bank of
Canada

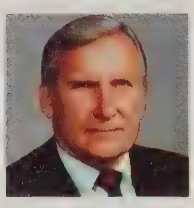
J. W. E. Mingo, Q.C.
Halifax
Barrister
Stewart MacKeen & Covert



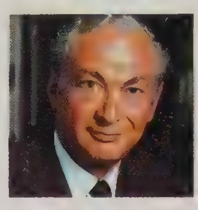
Pierre A. Nadeau
Montreal
Chairman of the Board
Tioxide Canada Inc.

J. Edward Newall
Mississauga
Chairman, President and Chief Executive Officer
Du Pont Canada Inc.

Paul Paré, O.C.*
Montreal
Chairman
Imasco Limited

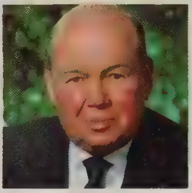


Ralph A. Pfeiffer, Jr.
Purchase, N.Y.
Retired Chairman
IBM World Trade Corp.



Neil F. Phillips, Q.C.
New York
Resident Senior Counsel
Phillips & Vineberg

Herbert C. Pinder
Saskatoon
President
Saskatoon Trading Company Limited



Claude Pratte, Q.C.
Quebec City
Counsel
Stein, Monast, Pratte & Marseille

Charles I. Rathgeb
Scarborough
Chairman
Comstock International Ltd.

Kenneth C. Rowe
Halifax
Chairman, President and Chief Executive Officer
I.M.P. Group Limited

Peter N. Thomson
New Providence, Bahamas
Chairman
West Indies Power Corporation Limited

John A. Tory, Q.C.
Toronto
President
The Thomson Corporation Limited

W. P. Wilder
Toronto
Chairman of the Board
The Consumers' Gas Company Ltd.

**Retiring December 2, 1986*
***Retiring January 7, 1987*

The five standing committees of the Board of Directors of The Royal Bank of Canada, as listed below, have the responsibility of maintaining integrity and sensitivity within the major areas of activity of the Bank, consistent with the strategic development goals of the corporation.

The Loan Policy Committee sustains an advisory and monitoring role with regard to the lending policies and practices of the Bank.

Chairman: F.B. Common, Jr.
Members: R.W. Campbell, G.C. Eaton, A.R. Haynes, P.L.P. Macdonnell, C.S. Malone, W.E. McLaughlin, J.W.E. Mingo, J.E. Newall, P.N. Thomson.

The Loan Policy Committee reviews and monitors the application of credit policy to ensure prudent risk management and consistent strategic planning. Loans of magnitude exceeding the generally acceptable percentage of capital, and those involving unusual circumstances are studied by the committee prior to management approval. Loans to directors and employees are approved by this group and, as required by the Bank Act, are reported to the Board of Directors. Finally, subject to the provisions of the Bank Act, administrative matters of an urgent nature may be referred to this committee for approval prior to subsequent review by the following meeting of the Board.

The committee meets regularly, twice a month, in addition to policy meetings and reports its activities to the Board with appropriate recommendations, desirable in the circumstances.

The Audit Committee assumes the responsibility of reviewing the audited annual financial statements and internal control procedures of the Bank, and of ensuring that disclosure of accurate, reliable data is made to interested parties.

Chairman: N.F. Phillips.
Members: I.A. Barclay, G.H. Blumenauer, A.B. Marshall, R.A. Pfeiffer, Jr., H.C. Pinder.

The Audit Committee, through meetings with shareholders' auditors, Chief Inspector and periodic reviews of internal control procedures and accounting practices of the Bank, ensures compliance with the law. Management information systems development and revisions to accounting practices are also subject to review by this committee.

The committee meets as required and at least three times annually. It reports to the Board of Directors on its activities, particularly its review of the Bank's financial statements and on the nomination and remuneration of auditors.

The Nominating Committee, under given criteria governing the overall composition of the Board, is elected to recommend suitable candidates for appointment as directors.

Chairman: Claude Pratte.
Members: R.W. Adam, Mitzi S. Dobrin, W.D.H. Gardiner, Paul Paré, C.I. Rathgeb.

The Nominating Committee, under guidelines established to sustain Board composition, reviews and recommends areas of representation which are complementary to the Bank's strategic development goals. The committee further seeks to identify candidates who are able and willing to participate in the diverse scope of the Royal Bank's activities.

The committee meets at least semi-annually and is required to report to the Board of Directors at least once each fiscal year.

The Personnel and Compensation Committee, in an advisory capacity, reviews and monitors Personnel policies, management development program and total compensation practices of the Bank.

Chairman: John A. Tory.
Members: John Anderson, J.A. Armstrong, W.F. Light, J.P. Maurer, W.P. Wilder.

The Personnel and Compensation Committee is charged with periodic reviewing of the Bank's long range plans and policies for recruiting, developing and motivating personnel. Compensation practices and management succession are areas of regular review and approval of remuneration of the Bank's most senior executive staff is required of this committee.

The committee is required to submit to the Board of Directors a report on its activities and any recommendations it deems appropriate.

The Public Policy Committee reviews the Bank's public posture to ensure that its operations remain consonant with the changing values and expectations of society.

Chairman: C.A. Dagenais.
Members: J.R. Evans, J.K. Finlayson, C.H. Knight, Dawn R. McKeag, P.A. Nadeau, K.C. Rowe.

The Public Policy Committee acts in an advisory capacity to the Board of Directors in areas relating to the Bank's overall interaction with its various key publics. Studies of the Bank's efforts to ensure ethical and socially responsible business conduct, corporate responsibility by way of both human resource and financial contributions, and the appropriateness of Public Affairs considerations as related to the Bank's strategic goals, form the key elements of this committee's functional mandate.

Reports and recommendations are made annually to the Board of Directors. Meetings are scheduled on a quarterly basis.

EXECUTIVE OFFICERS

Chairman & Chief Executive Officer
Allan R. Taylor (Toronto)
Vice-Chairmen
A.H. Michell
R.G.P. Styles (Toronto)
President
J.E. Cleghorn
Senior Executive Vice-President Credit
B.D. Gregson (Toronto)
Senior Executive Vice-President Investment Banking – North America & Treasury
R.C. Paterson (Toronto)
Senior Executive Vice-President Retail & Commercial Banking
M.J. Regan

HEAD OFFICE MANAGEMENT

Executive Vice-Presidents
B.V. Kelly (Toronto)
W.A.R. MacDonald
E.P. Neufeld (Toronto)
Senior Vice-Presidents
N.C. Achen (Toronto)
R.L. Arsenault
H.G. Buckrell
W.C. Bull
J.T. Burnett (Toronto)
J.P. Clarke
A. Cravero (Toronto)
W.R. Fithern
J.C. Grant (Toronto)
E.L. Grosland (Toronto)
R.A. Masleck (Toronto)
W.J. McCartney
P.J. Rossiter (Toronto)
J.C. Sinclair (Toronto)
E.G. Stone (Toronto)
R.J. Sutherland (Toronto)
Senior Vice-President & Treasurer
G.C. Aitken (Toronto)
Senior Vice-President & Chief Inspector
J.H.E. Bolduc
Senior Vice-President & Comptroller
D. D'Alessandro
Vice-Presidents
J.D. Anderson
M.A. Bastian (Toronto)
R. Bodt (Toronto)
A.A. Bowbyes (Toronto)
J.K. Breen (Toronto)
W.P. Carter
P.A. Case (Toronto)
B.D. Champion (Toronto)
W.B. Cockburn (Toronto)
M.A. Corlett (Toronto)
C.J. Coveyduck
A.R. Creasor
J. Driedger (Toronto)
J.B. Easton (Toronto)
H.E. Elsie (Toronto)
G.E. Farrow (Toronto)
E.D. Ferguson (Toronto)
V.T. Forster
J.M. Froese (Toronto)
J.J. Gannon
R. Gazard (Toronto)
G. Gill
B.M. Gray (Toronto)
H.C. Gregg (Toronto)
D.D.E. Grier (Toronto)
B.P. Griffiths (Toronto)
J.A.R. Guay
R.G. Hall (Toronto)
G.R. Heckman (Toronto)
A.J. Hogan
R.G. Hunkin
R.M. Juneau (Toronto)
W.K. Kellett (Toronto)
J.R. Klassen
F.H.S. Lablans
D.H. Loucks
J.K. MacKay
C.G. MacKenzie
B.C. Marshall
B.D. Marshall (Toronto)
T.R. McDermid
H.D. McRorie (Winnipeg)
K.J. Morrison (Toronto)
M.A. Nicolai (Toronto)
J.V. Oram (Toronto)
P.A. Palmer
G.H. Pickel
N.L. Rapkin
P.H. Rubenovitch
R.L. Spicer
W.D. Squires
H.C. Stewart
J.K. Talbot (Toronto)
R.E. Travis (Toronto)
P.H. Tucker (Toronto)
K.A. von dem Hagen (Toronto)
J.C. Walz (Toronto)
D.S. Wells
Vice-President & Chief Accountant
J. Merriam
Vice-President & Secretary
R.J. Moores

FIELD MANAGEMENT

Senior Vice-Presidents & General Managers
T.W. Bleackley (Vancouver)
G.J. Feeney (Halifax)
G.J. Johnson (Toronto)
D.N. Kitchen (Calgary)
W.C.C. Mackay (London, England)
J.G. Macpherson (Toronto)
J.B. McDonald (Winnipeg)
V.G. McKay (Hong Kong)
J.N.T. Rednall (Coral Gables, Florida)
R.B. Robertson (Regina)
M.L. Turcotte (Montreal)
J.M. Walker (New York)
Senior Vice-Presidents
M.C.S. Baptista (Toronto)
B.C. Galloway (Toronto)
W.J. Gorman (Toronto)
W.J.H. Nimmo (Toronto)
P.A. Taylor (London, England)
Vice-Presidents
D.M. Baxter (Calgary)
J.P. Béland (Montreal)
G.R. Bernard (Quebec City)
R.G. Bernard (Montreal)
J.G. Bisaillon (Montreal)
J.H.G. Camiré (Montreal)
A.M. Channell (Coral Gables, Florida)
J.T. Clayden (Tokyo, Japan)
C.S. Coffey (Toronto)
A.E. Colling (Toronto)
J.D. Davison (Toronto)
W.R. Dinwoodie (Chicago)
W.D. Dobson (Winnipeg)
B.W. Dorset (Calgary)
L.G. Edmonds (Vancouver)
J.R.J. Fauvel (Montreal)
C.L. Fong (Calgary)
G.F. Gaffney (Vancouver)
L.K. Gieck (Calgary)
W.H. Gilbert (Toronto)
G.D. Gillespie (London, England)
W.J. Grace (Toronto)
R.F. Gulliford (Toronto)
K.W. Harrison (Winnipeg)
R.A.R. Haskins (Vancouver)
R.F. Hemeon (Vancouver)
J.E. Henry (Calgary)
R.W. Hoke (New York)
J.E. Johannesson (Toronto)
A.L. Johnson (Toronto)
K.N. Kikano (London, England)
M.G. Klingsick (London, England)
R.P. Lasnier (Montreal)
E.W. Latimer (Burlington)
J.Y. Lawrie (Singapore)
J.M. Lejeune (Montreal)
K.A. Littlewood (Edmonton)
G.D. Loewen (Montreal)
E.J. Lundy (Vancouver)
F.G. MacDonald (Toronto)
I.A. MacKay (New York)
A.S. MacNeill (Ottawa)
A.A. McArthur (Houston, Texas)
E.R. McCutcheon (New York)
J.M. Messmer (Toronto)
S.A. Middaugh (Halifax)
W.T. Moodie (New York)
W.R. Penner (Vancouver)
H.A. Philpott (Regina)
M.D. Pollock (Vancouver)
A.L. Pottle (Halifax)
J.H. Prenger (Toronto)
P.J. Rafuse (Toronto)
D.L. Robertson (Toronto)
M.J. Ross (New York)
B. Schroder (Montreal)
D.R. Séguin (Montreal)
R.F.M. Smith (Calgary)
G.G. Tallman (Calgary)
A.L. Tower (Toronto)
J.A.B. Townley (London, England)
J.B. Traynor (Toronto)
A.G. van Schalkwyk (Toronto)
J.A.W. Van Slyck (San Francisco)
W.C. Watt (Regina)

SUBSIDIARIES & AFFILIATES *

Senior Vice-Presidents
W.J. MacKay (Melbourne, Australia)
P.A. Taylor (London, England)
A.A. Webb (Geneva, Switzerland)
Vice-Presidents
T.J. Betley (Guernsey, Channel Islands)
M.A. Brennan (São Paulo, Brazil)
J.R. Groves (Hong Kong)
J.E.D. Lepage (Brussels, Belgium)
R.H. Riviere (Melbourne, Australia)
K.A. Smee (San Juan, Puerto Rico)
G.C. Tibbatts (Melbourne, Australia)

**Seconded Royal Bank Executive Officers*

HEAD OFFICE

1 Place Ville-Marie
P.O. Box 6001
Montreal, Quebec
Canada H3C 3A9

BANKING NETWORK – FIELD HEADQUARTERS

Canada

Atlantic Provinces
5161 George Street
P.O. Box 1147
Halifax, Nova Scotia
B3J 2Y1
Senior Vice-President and General Manager
G.J. Feeney
140 branches
(New Brunswick–31,
Newfoundland–20,
Nova Scotia–83
Prince Edward Island–6)

Quebec
5 Place Ville-Marie
P.O. Box 6001
Montreal, Quebec
H3C 3A9
Senior Vice-President and General Manager
M.L. Turcotte
204 branches
(Quebec–203,
Northwest Territories–1)

Ontario–Metropolitan Toronto
20 King Street West
Toronto, Ontario
M5H 1C4
Senior Vice-President and General Manager
G.J. Johnson
190 branches

Ontario (excluding Toronto)
20 King Street West
Toronto, Ontario
M5H 1C4
Senior Vice-President and General Manager
J.G. Macpherson
346 branches

Manitoba
220 Portage Avenue
Winnipeg, Manitoba
R3C 2T5
Senior Vice-President and General Manager
J.B. McDonald
102 branches

Saskatchewan
2010-11th Avenue
Regina, Saskatchewan
S4P 3A2
Senior Vice-President and General Manager
R.B. Robertson
119 branches

Alberta
335 Eighth Avenue S.W.
Calgary, Alberta
T2P 2N5
Senior Vice-President and General Manager
D.N. Kitchen
161 branches
(Alberta–159,
Northwest Territories–2)

British Columbia
1055 West Georgia Street
Vancouver, British Columbia
V6E 3S5
Senior Vice-President and General Manager
T.W. Bleackley
180 branches
(British Columbia–179,
Yukon–1)

International

Latin America & Caribbean
2199 Ponce de Leon Boulevard
Coral Gables, Florida 33114-3806
U.S.A.
Senior Vice-President and General Manager
J.N.T. Rednall

U.S.A.
Park Avenue Plaza
55 East 52nd Street
New York, New York 10055
U.S.A.
Senior Vice-President and General Manager
J.M. Walker

DOMESTIC SUBSIDIARIES AND AFFILIATES

Royal Bank Mortgage Corporation
RoyLease Limited
1 Place Ville Marie
P.O. Box 6001
Montreal, Quebec
H3C 3A9

RoyNat Inc.
620 Dorchester Boulevard West
Montreal, Quebec
H3B 1P2

CORPORATE/INVESTMENT BANKING AND TREASURY

Corporate and Government Banking Field Headquarters

Canada
Royal Bank Plaza
200 Bay Street
Toronto, Ontario
M5J 2J5
Senior Vice-President
W.J.H. Nimmo

Europe
99 Bishopsgate
London EC2M 3XQ
England
Senior Vice-President
W.C.C. Mackay

Japan
14th Floor
Hibiya Kokusai Building
2-2-3 Uchisaiwai-Cho
Chiyoda-ku
C.P.O. Box 1709
Tokyo 100
Vice-President
J.T. Clayden

U.S.A.
Park Avenue Plaza
55 East 52nd Street
New York, New York 10055
Senior Vice-President
J.M. Walker

Investment Banking and Treasury Units

Canada
Investment Banking and Treasury Operations
The Royal Bank of Canada
200 Bay Street
Royal Bank Plaza
Toronto, Ontario
Senior Vice-President
B.C. Galloway

Europe
Orion Royal Bank Limited
1 London Wall
London EC2Y 5JX
England
Chairman & Chief Executive Officer
J.R. Sanders

Kitcat & Aitken & Co.
The Stock Exchange
London EC2N 1HB
England
Managing Director
P. Nuttall

RBC Gilts Limited
1 London Wall
London EC2Y 5JX
England
Managing Director
J. Doctor

The Royal Bank of Canada (Channel Islands) Limited
P.O. Box 48
St. Julian's Avenue
St. Peter Port, Guernsey
Channel Islands
Managing Director
T.J. Betley

The Royal Bank of Canada (Suisse)
Rue Diday 6
Case Stand 130
1211 Geneva 11
Switzerland
General Manager
A.A. Webb

Asia Pacific
Investment Banking and Treasury Operations
14th Floor
Hibiya Kokusai Building
2-2-3 Uchisaiwai-Cho
Chiyoda-ku
C.P.O. Box 1709
Tokyo 100
Japan
Vice-President
J.T. Clayden

Orion Royal Bank Limited
12th Floor
Hibiya Kokusai Building
2-2-3 Uchisaiwai-Cho
Chiyoda-ku
C.P.O. 1709
Tokyo 100
Japan
Chief Representative
J. Fawthrop

Orion Royal Pacific Limited
28th Floor, Alexandra House
16-20 Chater Road
Hong Kong
Managing Director
J.R. Groves

The Royal Bank of Canada Trust Company (Asia) Limited
18th Floor, Gloucester Tower
The Landmark
11 Pedder Street, Central
G.P.O. Box 3302
Hong Kong
Managing Director
R. Hoare

Affiliate
Capel Court Corporation Limited
425 Collins Street
Melbourne, VIC 3000
Australia
Deputy Managing Director
R. Chamberlain

Affiliate
China Investment and Finance Limited
2306-2309 Connaught Centre
1 Connaught Place
G.P.O. Box 11509
Hong Kong
Managing Director
R.B. Gray

U.S.A.
Investment Banking & Treasury Operations
68 William Street
New York, New York 10005
Vice-President
I.A. MacKay

Orion Royal Bank Limited
Park Avenue Plaza
55 East 52nd Street
New York, New York 10055

Latin America & Caribbean
Affiliate
RoyWest Trust Corporation (Bahamas) Limited
West Bay Street
P.O. Box N-7788
Nassau, N.P.
President and Chief Executive Officer
D.R. Kester

International Business Units

Antigua
Branch
25-26 High Street At Market
P.O. Box 252
St. John's

Argentina
Main Branch and Regional Office
Florida 202 Esq. Cangallo
Casilla de Correo 1899
Buenos Aires
(2 sub-branches in Buenos Aires)
Representative Office
Florida 234 Esq. Cangallo, 2° Piso
Casilla de Correo 1899
Buenos Aires

Australia
Affiliates
National Mutual Royal Bank Limited
425 Collins Street
Melbourne, VIC 3000

Capel Court Corporation Limited
425 Collins Street
Melbourne, VIC 3000

Bahamas
Regional Office
Beaumont House
327 Bay Street
P.O. Box N-7549
Nassau, N.P.
Main Branch
P.O. Box N-7537
323 Bay Street
Nassau, N.P.
(15 other branches/sub-branches in Bahamas)
Subsidiaries
Finance Corporation of Bahamas Limited
Frederick House
Frederick Street
P.O. Box N-3038
Nassau, N.P.

The Royal Bank of Canada International Limited
Beaumont House
P.O. Box N-3024
Nassau, N.P.
Affiliate
RoyWest Trust Corporation (Bahamas) Limited
West Bay Street
P.O. Box N-7788
Nassau, N.P.

Barbados
Regional Office
Trident House
Lower Broad Street
P.O. Bag Service 1011
Bridgetown
Main Branch
P.O. Box 68
Broad Street
Bridgetown
(5 sub-branches in Barbados)
Subsidiaries
The Royal Bank of Canada (Barbados) Limited
Royal Bank House
Bush Hill Garrison
St. Michael
P.O. Bag Service 1022
Bridgetown

Royal Bank (Barbados) Financial Corporation
Royal Bank House
Bush Hill Garrison
St. Michael
P.O. Box 626C
Bridgetown

Belgium
Subsidiary
The Royal Bank of Canada (Belgium) S.A.
Rue de Ligne 1
B-1000 Bruxelles

Belize
Branch
60 Market Square
P.O. Box 364
Belize City
(3 other branches in Belize)

Brazil
Representative Office
Av. Paulista 460, 16th Floor
01310 São Paulo

Subsidiary
Banco Royal do Canada (Brasil) S.A.
Av. Paulista 460, 16th Floor
01310 São Paulo

Main Branch
Banco Royal do Canada (Brasil) S.A.
Rua 15 de Novembro 240
Caixa Postal 8065
01310 São Paulo

Cayman Islands
Branch
P.O. Box 245
Cardinal Avenue
George Town
Grand Cayman

Affiliate
RoyWest Trust Corporation (Cayman) Limited
Cardinal Avenue
P.O. Box 707
George Town
Grand Cayman

Channel Islands
Subsidiaries
The Royal Bank of Canada (Channel Islands) Limited
Orion Royal Bank (Guernsey) Limited
The Royal Bank of Canada Trustees (Guernsey) Limited
The Royal Bank of Canada Trustees (Jersey) Limited
P.O. Box 48
St. Julian's Avenue
St. Peter Port, Guernsey

RBC Offshore Fund Managers Limited
P.O. Box 246
Ann's Place
St. Peter Port, Guernsey

China (People's Republic of)
Representative Offices
Shenzhen
Suite 1208
International Commercial Building
East Block
Shenzhen

Beijing
Room 5086, Beijing Hotel
Beijing

Colombia
Affiliate
Banco Royal Colombiano
Carrera 8 No. 14.45
Apartado Aéreo 3438
Bogotá 5

Commonwealth of Dominica
Branch
Bayfront
P.O. Box 19
Roseau

France
Subsidiary
The Royal Bank of Canada (France)
3, rue Scribe
75440 Paris
Cedex 09

Germany (Federal Republic of)
Subsidiary
The Royal Bank of Canada A.G.
P.O. Box 102247
Bockenheimer Landstrasse 61
D-6000 Frankfurt (Main) 1

Greece
Subsidiary
RoyMidEast Limited
Leoforas Kifissias 38
GR-151-25 Paradissos Amaroussion
Athens

Hong Kong
Branch
18th Floor, Gloucester Tower
The Landmark
11 Pedder Street, Central
G.P.O. Box 3302
Hong Kong

Subsidiaries
InchRoy Credit Corporation Limited
3908 Windsor House
311 Gloucester Road
P.O. Box 31386
Causeway Bay

Orion Royal Pacific Limited
28th Floor
Alexandra House
16-20 Chater Road, Central

The Royal Bank of Canada Trust Company (Asia) Limited
18th Floor, Gloucester Tower
The Landmark
11 Pedder Street, Central
G.P.O. 3302
Hong Kong

Affiliate
China Investment & Finance Limited
2306-2309 Connaught Centre
1 Connaught Place
G.P.O. Box 11509

India
Representative Office
N104 Panchshila Park
New Delhi 110017
India

Italy
Representative Office
Corso Matteotti 3
20121 Milano

Japan
Branch
14th Floor
Hibiya Kokusai Building
2-2-3 Uchisaiwai-Cho
Chiyoda-ku
C.P.O. Box 1709
Tokyo 100

Subsidiary
Orion Royal Bank Limited
Representative Office
14th Floor
Hibiya Kokusai Building
2-2-3 Uchisaiwai-Cho
Chiyoda-ku
C.P.O. 1709
Tokyo 100

Korea
Branch
Kyobo Building
7th Floor
1-1,1-Ka, Chongro
Chongro-Ku
C.P.O. Box 5374
Seoul

Lebanon
Subsidiary
The Royal Bank of Canada (Middle East) S.A.L.
Ghantous & Sons Bldg.
Dora Boulevard
Beirut

Mexico
Representative Office
Apartado Postal 6-1020
Hamburgo 172
Piso 5
Mexico 6 D.F.

Montserrat
Branch
Parliament Street
P.O. Box 222
Plymouth

The Netherlands
Subsidiaries
RBC Finance B.V.
Keizersgracht 604
1017 EP Amsterdam

Orion Leasing Nederland B.V.
Herengracht 489
1017 BT Amsterdam

Puerto Rico
Main Branch and Regional Office
255 Ponce de Leon Avenue
P.O. Box 819
Hato Rey
(4 other branches in Puerto Rico)
Subsidiary
Royal Bank de Puerto Rico
654 Munoz Rivera Avenue
G.P.O. Box 4208
Hato Rey
(16 other branches in Puerto Rico)

St. Kitts
Branch
Fort & Bay Roads
P.O. Box 91
Basseterre

St. Lucia
Branch
Boulevard & Laborie Streets
P.O. Box 280
Castries

Singapore
Branch and Asian Currency Unit
140 Cecil Street #01-00
PIL Building
Singapore 0106
Subsidiary
The Royal Bank of Canada
(Asia) Limited
140 Cecil Street #16-01
PIL Building
Singapore 0106

Spain
Representative Office
Paseo de la Castellana 51.4a
28046 Madrid

Switzerland
Subsidiaries
The Royal Bank of Canada (Suisse)
Rue Diday 6
Case Stand 130
1211 Geneva 11

RoyCan Trust Company S.A.
15, Rue Pierre Fatio
1204 Geneva
Affiliate
RoyWest Trust Corporation S.A.
Lausanne
C.P. 120, Avenue d'Ouchy 41
1000 Lausanne 13

Taiwan
Branch
8th Floor
Tun Hwa Financial Building
214 Tun Hwa North Road
P.O. Box 81-775
Taipei 100

Trinidad
Affiliates
The Royal Bank of Trinidad and
Tobago Limited
3B Chancery Lane
P.O. Box 287
Port of Spain

Royal Bank Trust Company
(Trinidad) Limited
55 Independence Square
Port of Spain

The Royal Bank Mortgage and
Finance Company Limited
55 Independence Square
Port of Spain

United Arab Emirates
Branch
P.O. Box 3614
4th Floor
Chamber of Commerce Building
Deira, Dubai

United Kingdom
Main Branch
6 Lothbury
London EC2R 7JY
(1 other branch in London)
Subsidiaries
Kitcat & Aitken & Co.
The Stock Exchange
London EC2N 1HB

Orion Royal Bank Limited
Orion Leasing Holdings Limited
RBC Gilts Limited
1 London Wall
London EC2Y 5JX

The Royal Bank of Canada Forfait
Finance Limited
The Royal Bank of Canada Trade
Finance Limited
1 Seething Lane
London EC3N 4BP

Western Trust & Savings Limited
The Moneycentre
Plymouth PL1 1SE
Affiliate
Libra Bank PLC
140 London Wall
London EC2Y 5DN

U.S.A.
Agencies
Miami
801 Brickell Avenue
Suite 1001
Miami, Florida 33131
San Francisco
101 California Street
Suite 2000
San Francisco, California
94111-5880
Branches
New York
68 William Street
New York, New York 10005
Portland
1515 South West 5th Avenue
Suite 900
Portland, Oregon 97201

Representative Offices
Chicago
33 North Dearborn Street
Suite 1200
Chicago, Illinois 60602
Dallas
4380 Thanksgiving Tower
1601 Elm Street
Dallas, Texas 75201
Denver
1801 Broadway
Suite 300
Denver, Colorado 80202
Houston
Texas Commerce Tower
Suite 6850
600 Travis Street
Houston, Texas 77002
Los Angeles
600 Wilshire Boulevard
Suite 600
Los Angeles, California 90017
Pittsburgh
600 Grant Street
Suite 4970
United States Steel Building
Pittsburgh, Pennsylvania 15219
San Francisco
101 California Street
Suite 2000
San Francisco, California 94111-5880
Subsidiaries
The Royal Bank and Trust Company
68 William Street
New York, New York 10005

Orion Royal Bank Limited
Representative Office
Park Avenue Plaza
55 East 52nd Street
New York, New York 10055

Venezuela
Representative Office
Edificio Banco Royal Venezolano
C.A.
Piso 8
Esquina de Animas y Avenida
Urdaneta
Apartado 1480
Caracas 1010A

Geographic Breakdown of Common Shareholders
October 31, 1986

	Holders	Per Cent	Shares 000's	Per Cent
Newfoundland	218	0.2%	80	0.1%
Nova Scotia	4,987	5.6	5,498	5.2
P.E.I.	293	0.3	220	0.2
New Brunswick	1,057	1.2	657	0.6
Quebec	51,185	57.0	22,412	21.0
Ontario	19,831	22.1	64,989	61.0
Manitoba	1,587	1.8	1,136	1.1
Saskatchewan	909	1.0	589	0.6
Alberta	2,332	2.6	1,762	1.6
British Columbia	4,726	5.3	3,534	3.3
N.W.T. & Yukon	32	–	5	–
Sub-Total Domestic	87,157	97.1	100,882	94.7
U.S.A.	1,104	1.2	1,542	1.5
Other Foreign	1,491	1.7	4,098	3.8
Total	**89,752**	**100.0%**	**106,522**	**100.0%**

Classification of Common Shareholders by Size of Holding
October 31, 1986

1 to 99	37,789	42.1%	985	0.9%
100 to 999	45,453	50.6	12,737	12.0
1,000 to 9,999	6,055	6.8	12,829	12.0
10,000 to 99,999	368	0.4	9,358	8.8
100,000 & Over	87	0.1	70,613	66.3
Total	**89,752**	**100.0%**	**106,522**	**100.0%**

Classification of Common Shareholders by Type
October 31, 1986

Individuals	82,049	91.4%	21,793	20.5%
Institutions	5,912	6.6	32,199	30.2
Others (Incl. Nominees)	1,791	2.0	52,530	49.3
Total	**89,752**	**100.0%**	**106,522**	**100.0%**

Share Price Ranges

Class of Shares		*1986*	
	High	*Low*	*Close*
Common Shares	$35.25	$27.50	$33.25
First Preferred Shares			
Series A ($1.88)	$25.13	$22.88	$24.00
Series B ($1.45)	$19.13	$17.00	$18.75
Series C (Floating Rate)	$100.44	$99.00	$100.00
Series D ($U.S. Floating Rate)	$102.00	$101.40	$101.50
Series E (Price-Adjusted Floating Rate)	$101.00	$99.50	$100.50
Second Preferred Shares			
Series A ($2.75)	$33.88	$30.25	$32.25

Stock Exchange Listings

Canada: Montreal, Toronto, Vancouver, Winnipeg and Alberta Stock Exchanges

Japan: Tokyo Stock Exchange

Switzerland: Basle, Geneva, Zurich

U.K.: London Stock Exchange

Transfer Agent and Registrar

Main Agent:

Mailing Address:	Montreal Trust Company of Canada P.O. Box 1900, Station "B" Montreal, Quebec Canada H3B 3L6
Street Address:	1 Place Ville Marie Montreal, Quebec Canada
Telephone:	(514) 397-7000
Telex:	055-61286

Co-Agents *(Canada)*
Montreal Trust Company of Canada

Halifax, N.S. 1690 Hollis Street P.O. Box 2187 B3J 3C5	Toronto, Ontario 15 King Street W. M5H 1B4
Calgary, Alberta 411-8th Avenue S.W. T2P 1E7	Regina, Sask. 1908-11th Avenue P.O. Box 4500 S4P 3W7
Winnipeg, Man. 221 Portage Avenue P.O. Box 369 R3C 2J1	Vancouver, B.C. 510 Burrard Street V6C 3B9

Co-Agent *(United Kingdom)*

The Royal Bank of Canada
6 Lothbury
London, England
EC2R 7JY

Shareholder Dividend and Share Purchase Plan

Shareholders of record or beneficial owners of Common and/or of certain eligible series of preferred shares may enroll in the Plan. Participants in the Plan may elect to receive their dividends in the form of new Common Shares (stock dividends) or reinvest their cash dividends in new Common Shares. In both instances, the price of the new Common Shares is 95% of the average market price determined at the date of the dividend payment. Participants in the Plan may also make optional payments to purchase new Common Shares as frequently as once a month (on the Investment Date) for an aggregate amount up to Cdn. $7,500 per quarterly dividend period at 100 per cent of the average market price.

Further information on the Shareholder Dividend and Share Purchase Plan may be obtained from the Manager, Shareholder Services, at the Bank's corporate headquarters.

Direct Deposit Service

Shareholders and debentureholders may also elect to have their dividends or interest deposited directly into their savings or chequing accounts at any financial institution which is a member of the Canadian Payments Association. To arrange, please write to the Manager, Shareholder Services, at the Bank's corporate headquarters.

Institutional Investor, Broker, Security Analyst Contact

Institutional investors, brokers, security analysts and others desiring financial information about the Bank should contact the Manager, Investor Relations, at the Bank's corporate headquarters.

Duplicate Annual Reports

Some registered holders of shares of The Royal Bank of Canada might receive more than one copy of shareholder information mailings such as this Annual Report. While every effort is made to avoid duplication, if securities of the same class or series are registered in different names and/or addresses, multiple copies are forwarded. Shareholders receiving more than one copy are requested to write to the Manager, Shareholder Services, at corporate headquarters so that arrangements may be made to avoid duplicate mailings.

Information concerning the Royal Bank and its activities in Canada and abroad may be obtained from the Public Affairs Department, at the Bank's corporate headquarters.

Mailing Address:	The Royal Bank of Canada P.O. Box 6001 Montreal, Quebec Canada H3C 3A9
Street Address:	1 Place Ville Marie Montreal, Quebec Canada
Telephone:	(514) 874-2110
Telex:	055-61086

Credits

Design: Taylor & Browning Design Associates, Toronto

Photography: Principal photography, Paul Orenstein, Paul Orenstein Photography Ltd., Toronto; Portraiture – Brian Willer, Toronto; Al Gilbert, FRPS, Toronto

Translation: Translatec, Montreal

Typography: Cooper & Beatty, Limited, Toronto; Typographic Centre, Montreal

Colour Separations: Empress Graphics Inc., Toronto

Printing: Arthurs-Jones Lithographing Ltd., Toronto

La Banque Royale publie son rapport annuel en français et en anglais. Pour obtenir un exemplaire de la version française, veuillez écrire à:

Service des affaires publiques
La Banque Royale du Canada
C.P. 6001
Montréal (Québec)
Canada H3C 3A9

Legal Deposit, 4th quarter 1986
Bibliothèque nationale du Québec

Printed in Canada


THE ROYAL BANK
OF CANADA